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COPYRIGHT ARBITRATION ROYALTY PANEL

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In the matter of:	Docket No. 2000-9
Digital Performance Right in Sound Recording and Ephemeral Recording	CARP DTRA 1 & 2

CARP Hearing Room
LM-414
Library of Congress
Madison Building
101 Independence Ave, SE
Washington, D.C.

Monday
July 30, 2001

The above-entitled matter came on for hearing, pursuant to notice, at 1:00 p.m.

BEFORE

THE HONORABLE ERIC E. VAN LOON Chairman
THE HONORABLE JEFFREY S. GULIN Chairman
THE HONORABLE CURTIS E. von KANN Arbitrator

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C-O-N-T-E-N-T-S

P-R-O-C-E-E-D-I-N-G-S

(1:08 p.m.)

MR. ROBERTS: Good afternoon, everyone. My name is Bill Roberts. I am senior attorney for Compulsory Licenses here at the Copyright Office. And on behalf of myself, Tanya Sandros in the back, Rita Ginnfredda, and our General Counsel David Carson and the Register of Copyrights, Marybeth Peters, and the Librarian of Congress, Dr. James Billington, I welcome all of you to the beginning of our proceeding to decide rates and terms for the digital performance right in sound recordings and ephemeral recordings.

Today begins the 180-day arbitration period, and on or before the 28th of January of next year, our arbitrators will deliver to us, the Copyright Office and the Library, a written decision detailing their findings of fact and conclusions of law and the terms and rates that they have deemed appropriate to assess.

At that point in time, the Register of Copyrights will review the decision and make her recommendation to the Librarian of Congress. And the

Librarian will publish his final decision. That will be either 60 days after the 28th of January if the Librarian accepts the Panel's decisions. If he determines that he needs to reject the Panel's decision and substitute his own decision, then it will be 90 days after the issuance of the decision on or before the 28th of January.

I'd like to introduce to you our arbitrators. Serving as our Chairperson, from Boston, Massachusetts, Eric Van Loon. Sitting to his immediate left, from Baltimore, Maryland, Jeffrey Gulin, and to Eric's right, from Washington, D.C., Curtis von Kann. These will be our arbitrators for the next 180 days.

I guess somewhat regret to inform all of you that there -- before opening statements can begin today there is a matter of resolving certain material that's going to be presented in these opening statements that is being deemed by at least one side to be confidential. And that means I am going to have to ask all of you in the room who are not associated with Counsel on the one side for broadcasters and

webcasters or the Recording Industry Association on the other to please temporarily leave this room so that Counsel may make their arguments and this decision may be made on this material, at which point you can return, and the arbitrators will begin this proceeding with opening statements. So thank you very much.

(Whereupon, the foregoing matter went off the record at 1:11 p.m. resumed immediately in Closed Session.)

CHAIRPERSON VAN LOON: Well, good afternoon, everyone, and welcome to this opening public session of our CARP deliberations on rates and terms for performance rights in digital recordings. We are here in the early days of what is currently a small industry of webcasting and broadcasting and are looking forward to hearing from the parties evidence and information about the state of the industry and all of the rest.

The Arbitration Panel, in looking at a variety of different stars or touchstones for things that might guide us, found a royalty decision written by Judge Learned Hand more than 50 years ago, in which he wrote that "The whole notion of a reasonable royalty it's a device in the aid of justice." He said, "It's a device by which that which is really incalculable shall be approximated." So we're guided, in part, by his point of view and in much more significant measure by what we will be hearing from you.

It's important for us to announce and explain briefly to the audience, now that we're back

on the record, that the hearings of the CARP Panel, Arbitration Panel, are open, public hearings for the largest extent. But that there is a provision for closed meetings under certain circumstances under Section 251.13 and 14 of the Federal Regulations. And that in order to consider a motion and deliberate on a motion, the Panel has voted three to -- unanimously that it was appropriate to close our opening statement -- or opening session briefly under 251.13(d), relating to matters that arguably involve privileged or confidential trade secrets or financial information. And so that's the legal basis for closing that. And I'm informed that for a short part of the opening statements later this afternoon, there will be similarly a closed session to address this.

Stemming from previous discussion with the parties here a month ago in a procedural hearing or meeting, it's been determined that each side will have approximately up to two hours to make their opening presentation. That will be divided, in some cases, among various spokesperson for the different sides. And we'll be hearing, we understand, first from the

copyright owners and performers.

And in the aid of our reporter, we would ask everyone to please identify yourself so we can also get to know you better.

MR. GARRETT: Mr. Chairman, members of the Panel, I'm Bob Garrett, along with my colleagues from Arnold and Porter. We represent the Recording Industry Association of America, RIAA. Good afternoon, and thank you for holding this hearing in the afternoon. It is one less day that I will spend up in the Library of Congress' cafeteria over the next seven weeks.

I put up some slides here and would like to just pass out copies for the arbitrators and other people in the room here for those who can't see it.

What I'd like to do during my opening statement, Your Honors, is cover, basically five topics. The first is the background and purpose of this proceeding. The second is the statutory standard that will guide your deliberations in this case. Third, I'd like to compare the approach that we've taken in our direct case with the approach that the

webcasters have taken in their case.

Next, I'd like to discuss the rulings of both another CARP and the Librarian in the Subscription Services decision. That was the first proceeding in which a CARP set royalty rates for a digital performance right and sound recordings. And, finally, I'd like to spend a little time just comparing our rate with the rate that has been proposed by the webcasters.

If you turn on your radio, conventional radio, you'll probably get somewhere between three or four, maybe as many as 20 or 30 different channels of music depending where you're located in this country. Depending upon the reception in that geographic area, you can get more or fewer channels. But if you turn on your computer and you go to the Internet, you can receive literally thousands of channels of highly themed, preprogrammed music, and that's true regardless of where you are. And depending upon the nature of your connection to the Internet, that music may sound exactly like the CD that you play on your stereo.

Now, for example, if you like jazz, and you live here in the D.C. area, you might be able to get two or three different local jazz stations just off the air. But on the Internet, you can go to the web sites of AM and FM radio stations from New Orleans, Chicago, all over the country, and on many of those web sites you're going to be able to hear exactly the same music, the same jazz programming that those stations offer over the air.

There are also web sites that you can listen to jazz channels, and those -- you can listen to music channels that are available only on the Internet. For example, one of the parties in this case, AOL, offers a music service known as spinner.com. And Spinner has over 200 different channels of preprogrammed music.

This slide here is from a page on the Spinner web site. If you go to the menu on the left and click on jazz and blues, the menu on the right will pop up, and you can see you get a listing of 24 different categories of jazz and blues. You click on any one of those categories and you can listen to

music from that category, one song after another, 24 hours a day, seven days a week.

Now, Spinner, of course, is but one service that provides preprogrammed music solely over its web site. There are many other such web sites with additional categories and sub-categories of not only jazz but all sorts of different types of music.

Now, these channels don't appear on web sites by magic. There are entrepreneurs out there who have put these channels on the web, and we call them webcasters. Spinner is an example of a webcaster, and likewise a radio station when it simulcasts a signal over the Internet is a webcaster. Now, these entrepreneurs are not compelled to use our recorded music. They can choose from all sorts of different content on which to build their businesses. But they choose our sound recordings; in fact, they choose the best of our sound recordings. And why? Because they believe that those sound recordings will help attract visitors to their web sites. And that's what their businesses depend on -- attracting visitors to their web sites.

Now, the recorded music on those channels doesn't appear magically either. It exists only because of the very significant efforts of both record labels and recording artists. It exists because hundreds of different record labels throughout this country are willing to incur the substantial risks of discovering, financing, and promoting recording artists. And they exist because those artists have the creative genius that is necessary to transform the notes and lyrics that you find on a piece of paper into a compelling performance that touches the emotions of a diverse group of people worldwide.

And while the financial rewards can be very great for a select group of sound recordings, the cost of running our business are enormous. As you will hear from one of our witnesses, the major record labels alone have spent literally billions of dollars creating the sound recordings that then form the basis of the businesses that the webcasters engage in.

Now, we own the property right, the copyright in hundreds of thousands of different sound recordings. And a very fundamental right of property

ownership in this country is the right to insist that others negotiate with the property owner before making commercial use of their property. Now, we don't have that right when it comes to the types of webcasting services that are involved in this case here. And that's because the law, specifically the Digital Millennium Copyright Act, or DMCA, affords these services a compulsory license.

Now, they can compel us to license them all of our copyrighted sound recordings without having to negotiate with us. All they've got to do is file a piece of paper over here at the Copyright Office and then they can transmit over the Internet hundreds of thousands of sound recordings that cost billions of dollars to create and to produce.

Now, we don't have control over the use of our property, but we do have one very basic right, and that is the right to receive the same level of compensation that we would have received had we been able to negotiate with the webcasters in a free marketplace, absent the compulsory license.

And that brings us to why we are here

today and what it is that you must do. And very simply, you must determine the level of compensation that we would have received in a free marketplace negotiation for the licenses at issue. Specifically, the Panel must set rates and terms for three statutory or compulsory licenses.

The first is the Section 114 license that actually permits the webcasters to transmit or to stream sound recordings over the Internet. And we call this the webcasters performance license. Secondly, Section 112 permits webcasters to make multiple copies of those sound recordings. And those copies are what the webcasters actually transmit over the Internet. Now, a webcaster doesn't always need to make multiple copies, but having those copies can make its business much more efficient. And the license that allows them to do that without our consent is the 112 ephemeral license, or the 112 webcaster ephemeral license.

There's a third license that does not directly involve webcasting but for which you must also set rates and terms. And that license is also

found in Section 112, and it permits certain background music services to make temporary copies of sound recordings in order to transmit those recordings to various business establishments. We call this the business services or the business establishment ephemeral license, and I'll discuss that briefly at the end of my statement here.

You also must set rates and terms for two periods of time: November 1998 to December 2000 and January 20001 to December 20002. However, I think it's worthy to note that neither side is offering a rate proposal that distinguishes between these two time periods.

That brings me to the statutory standard. Initially, there was a dispute between us and the webcasters over the standard that you are required to apply in setting rates and terms in this proceeding. The Copyright Office, however, in its July 16 order, resolved that dispute. It provides you with guidance that we believe is correct and that you must follow.

And let me emphasize a couple of points about the standard. First, the standard you must

apply in setting Section 114 rates and terms is the willing buyer/willing seller standard. The precise language is shown in the next slide here. It says, "The CARP shall establish rates and terms that most clearly represent the rates and terms that would have been negotiated in the marketplace between a willing buyer and a willing seller.

Now, here's what the Copyright Office said about that standard. It's on page 5 of its July 16 order. It said, "The statutory standard set forth in Section 114(f)(2)(b) requires the Panel to determine the rates that a willing seller and a willing buyer would agree upon through voluntary negotiations in the marketplace. And the Panel must use the willing seller/willing buyer standard to set rates for all non-interactive, non-subscription transmissions made under Section 114 license, including those within 150 miles of the broadcaster's transmitter. That 150 mile reference, we think, is significant, and I'll talk a little bit more about that later.

But the most important point here is to emphasize that that willing buyer/willing seller

standard is really the polestar that you must follow in this proceeding. And it is a polestar that emphasizes marketplace negotiations. This is essentially a fair market value test, because fair market value has traditionally been defined as what a willing buyer and a willing seller would agree to in a marketplace transaction. Now, that test is also, as one of our witnesses will explain, the same test that has historically been applied in other intellectual property cases, primarily patent cases, to determine a reasonable royalty.

Well, what does this mean for the webcaster performance license? We'll tell you what we think it means. We believe that your focus must be on discerning the rates and terms that would result in negotiations in a free market, absent the compulsory license. We believe that you must replicate a hypothetical negotiation where the willing seller is the record industry, and the willing buyers are webcasters. That negotiation must be for the non-inclusive right to transmit digitally all copyrighted sound recordings over the Internet and in a manner

You must consider any evidence which shows how a willing buyer and a willing seller would value the licenses at issue here.

There's a third point to emphasize about Section 114, and that is that the structure of Section 114 is very similar to the structure of Section 119, which is the satellite carrier compulsory license. This next slide quotes the relevant language from those two sections. And the Copyright Office also noted in its July 16 order, it said that the Panel should look to the Librarian's Section 119 decision for further guidance implementing the willing buyer/willing seller standard. I would add that you should also look at the CARP report, and that the Librarian affirmed, in the Section 119 proceeding, and I think you'll hear more about that as we go through this proceeding.

Finally, let's take a look at Section 112. Like Section 114, Section 112 also contains a willing buyer/willing seller standard. It says that the CARP shall establish rates that most clearly represent the fees that would have negotiated in the marketplace

that effectively provides each consumer with access to literally thousands of narrowly tailored channels of music.

The second point I want to emphasize about Section 114 relates to the following language. This language identifies certain types of evidence that you must consider in this proceeding -- evidence of promotion, substitution, relative contributions. Here's what the Copyright Office said about this provision. The exact language is on the slide. I think what it makes clear is that promotion, substitution, relative contribution, these are not separate standards. They're not separate standards that are co-equal with the willing buyer/willing seller standard. They're simply types of evidence that you must consider. And you must consider them only to the extent that they shed light on what it is that a willing buyer and a willing seller would negotiate in a free marketplace.

Now, furthermore, promotion, substitution, relative contributions are not the only types of evidence that you must consider in this proceeding.

between a willing buyer and a willing seller. The language is actually slightly different than Section 112, but the key is that it still refers to the willing buyer and the willing seller.

And here's what the Copyright Office said on page 5 of its July 16 order about 112. It said, "The standard for setting royalty fees for the Section 112 license is identical to the standard used to set rates for the Section 114 license. Now, rates should be set for the making of ephemeral recordings after full consideration of all evidence that relates to the marketplace value of these reproductions."

Now, what does this mean? One example I'll give you, webcasters in this case argue that the Section 112 rate should effectively be zero. The business services also have said that they should pay nothing, although they then go on to offer what we consider to be a token fee. And what these parties will have to show is that in the free market, absent the compulsory license, the Section 112 rates essentially have no value, that record companies would give these rights away for free. Now, we don't

believe the record is going to show that. We believe the Section 112 rights are valuable rights, and that those who want them must pay a marketplace price for them.

Let me move now to the next section of my opening statement, which is to talk a little bit about the different direct cases that each side has put in. As you know, Section 114 directs the parties to enter into voluntary negotiations over rates and terms. Section 112 contains a similar directive. And pursuant to that directive, RIAA established a Negotiating Committee that was comprised of members of a number of different record companies. And this included each of the major record companies, which collectively account for about 85 percent of the market.

And several of the members of that Negotiating Committee will testify before you over the next couple of weeks. These are the individuals at the record labels who have substantial experience negotiating licensing agreements for both new media and in many cases traditional media.

The Committee originally sought to negotiate with the trade association that represents the webcasters, DMA, or the Digital Media Association. DMA, however, told RIAA that DMA could not negotiate on behalf of its members. It told RIAA to negotiate with webcasters individually, and that's what RIAA did. It began what has become a very arduous, time consuming, and costly task of going to individual webcasters and attempting to negotiate deals with them for the Section 112 and 114 rates.

Its objective in these negotiations was to make deals, deals that the parties would consider to be fair and reasonable and that would ultimately form the basis of an industry-wide settlement, and that would avoid the need for this very hearing. Now, obviously, we were not successful in avoiding this hearing, but we have been successful in negotiating a number of different agreements.

Now, in some cases, those negotiations were completed in a matter of a few days or a few weeks. In other cases, they stretched over months. In the end, however, we were able to reach agreement

with several webcasters as to what are fair and reasonable rates and terms for the Section 112 and 114 licenses. And in the process, I think we learned a good deal about what it takes to be a willing buyer and a willing seller in this marketplace.

Now, when we filed our direct case, we had 25 agreements. Since then we have entered into a licensing agreement with one other webcaster in this proceeding. And we continue to negotiate with others who are willing to negotiate with us. We've included all 25 of the agreements in the record and will ask for permission to include the 26th as well. The next slide here identifies 26 licensees and the dates of the agreements that we reached with them.

Our position, bottom line, is that the rates and terms in these 26 agreements provide the best evidence of the willing buyer/willing seller rates and terms that the CARP must adopt in this proceeding. Why do we say that? Well, primarily because the RIAA agreements involve the same parties, the same right, the same works, the same medium, the same programming as the marketplace that the Panel

here must replicate.

We're not saying that the Panel ought to adopt the rates and terms in these 26 agreements simply because they do involve the same parties, the same right, the same medium, the same programming. The bulk of our case is going to be devoted to explaining why those rates and terms, the ones that we have negotiated in the marketplace, are consistent with what is going on in that marketplace, in particular, what the new and traditional media are spending for analogous rights, what we are spending to create copyrighted works, and what the webcasters themselves are spending on other parts of their businesses.

I think to determine willing buyer/willing seller rates, you need to understand the record business, and you need to understand the webcasting business. Why? Simply because those are the two willing buyers and the willing sellers in the negotiation that you must replicate. I think you've also got to understand the music publishing business and how that business differs from the record

business, and that's because the webcasters base their case on the flawed notion that these two businesses, the record business and the music publishing business, are interchangeable, that they would charge essentially the same marketplace rates for the separate rights that they own.

And what our case is really intended to do is to help you understand our business, the webcasters' business, the music publishing business, and, most importantly, how we license both new and traditional media rights for sound recordings. A substantial portion of our case is going to be devoted to describing agreements that not only RIAA has negotiated but that our individual companies have negotiated involving analogous rights outside the statutory license to both new and traditional medium.

And we're going to present that case through 17 witnesses. The majority of our witnesses have a substantial amount of experience in the record industry. Many of these witnesses also have a significant amount of experience in dealing with webcasters and new media licensing. Others have

experience in the music publishing business.

We have laid out in our pre-hearing memorandum a brief summary of the witnesses' testimony. I'm not going to repeat that summary here, but I do just want to highlight the testimony of three of our experts. One is Robert Yerman of LECG. Mr. Yerman has frequently been called upon to value different types of intellectual property using the same willing buyer/willing seller test that you must apply here. He's going to discuss with you how that willing buyer/willing seller test has been applied in other intellectual property cases, and he will show how that test would be applied here, explaining in particular the importance of negotiated agreements involving the same works and the same rights.

Another of our experts is Dr. Thomas Nagle of the Strategic Pricing Group. Dr. Nagle is a nationally recognized expert on pricing strategies. He and his consultant firm, SPG, are frequently called upon by clients in a wide variety of fields to help determine fair market value prices. And not for purposes of litigation but for purpose of running

their own businesses on a day-to-day basis. Using the economic analysis that Dr. Nagle and SPG traditionally apply in assisting these other businesses, he will show that the rates proposed by RIAA, in this case, are within the range of fair market value rates.

Our third expert is Dr. Steven Wildman of Michigan State. He's testified previously in our CARP proceedings concerning benchmarks for rate setting. He testified for the Recording Industry Association in the subscription services proceeding, and he's also testified for the broadcasters in other proceedings before the CARP and the Copyright Royalty Tribunal. What his testimony will show is that musical work rates are not appropriate benchmarks for setting sound recording rates. And he's also going to talk about why the decision in the 1997 subscription services proceeding is not an appropriate benchmark in this proceeding.

And as you will see, there are some very fundamental differences between our case and the case that the webcasters are putting on. The centerpiece of the webcasters' case is a study submitted by Adam

Jaffe. And it's important that you understand exactly where and how Dr. Jaffe calculates his proposed royalties. This study does not look at a single agreement involving sound recordings or a single agreement involving record companies or a single agreement involving webcasters. His study is based on what certain over-the-air radio stations supposedly pay to ASCAP, BMI, and SESAC, pursuant to certain agreements. To put it in other terms, the webcasters are also basing their case on agreements, but their agreements are very different than the agreement we believe that you must replicate here.

And remember your statutory mandate. You must adopt rates and terms that most clearly reflect or represent the rates and terms that a willing buyer and a willing seller would agree to in a free marketplace. Now, we don't believe that that means any buyer and any seller, for any rights involving any works and any medium and any programming. Rather, we believe that your focus must be on discerning the rates and terms that would result from negotiations in a free market, absent the compulsory license, that you

must replicate a hypothetical negotiation where the willing seller is the record company, and the willing buyers are the webcasters, and that that negotiation must be for the non-inclusive right to transmit digitally all copyrighted sound recordings over the Internet and in a manner that effectively provides each consumer access to literally thousands of highly themed music channels.

Professor Jaffe does not look at agreements that were negotiated in a free market, absent compulsory licensing. He looks at agreements that were negotiated, pursuant to a consent decree and subject to rate court supervision. He does not look at the license fees that the record industry charges. Instead he looks at the license fees that the music publishers charge. And he doesn't look at what webcasters pay; he looks at what a committee comprised of radio station representatives agreed to pay. And he doesn't look at what's paid for sound recordings; he looks at what's paid for musical works. He does not look at what's paid for digital rights, but he looks at what was paid for analog rights.

And he does not look at what is paid for rights to transmit across the United States over the Internet, but for the right to transmit on local, over-the-air radio stations with limited geographic reach. And, finally, he does not look at what is paid for rights which permit a consumer to receive literally thousands of channels of highly themed music, but rather for rights which permit consumers to receive a relative handful of generalized radio stations.

And these are all critical differences between the agreements on which Professor Jaffe relies and the agreements on which we rely. More importantly, these are all critical differences from the negotiations that you, the Panel, must replicate. And the significance of each of these differences will become even more apparent as we go through the next couple of weeks of testimony.

Let me also note that NPR has submitted a separate study, but it suffers from exactly the same flaws as the webcasters'. It's based solely on the musical work fees that public broadcasters pay ASCAP,

BMI, and SESAC, pursuant to a prior decision of a Copyright Arbitration Royalty Panel.

Now, you will hear the webcasters argue that our agreements do not reflect the willing buyer/willing seller test, that they do not reflect a fair market value. In one respect, I agree with them, although not for a reason that I expect they will say. None of the RIAA agreements was negotiated in a truly free marketplace. They were negotiated against the backdrop of a compulsory license. Now, in true marketplace negotiations, the buyer must reach an agreement with the seller or else that buyer will not have access to the seller's product.

Now, that's not the situation here. The record labels cannot withhold their sound recordings from webcasters who want to use them in accordance with the DMCA. As long as the webcaster complies with the statutory requirements, we are compelled to license our sound recordings to them. And if the webcaster refuses to pay what we consider to be a fair and reasonable royalty rate, we've got to come to you. And all the while that this proceeding goes on, they

can continue to use the sound recordings as long as they do so in accordance with the DMCA.

Now, as the Librarian said in the most recent 1-18 CARP proceeding, it is difficult to understand how a license negotiated under the constraints of a compulsory license, where the licensor has no choice but to license, could truly reflect fair market value.

Now, as this suggests, it is normally the copyright user in a CARP proceeding, and not the copyright owner, who points to the rates and voluntary agreements. That was, of course, the case in the last 1-18 proceeding. And the reason is because they know, the copyright user knows, that they have the advantage where the copyright owner is effectively forced to sell.

Now, think about this from the viewpoint of the webcaster. He doesn't need to negotiate before using our sound recordings. All he has to do is file a piece of paper with the Copyright Office. If he negotiates an agreement with us, he's got to begin paying us. But if he doesn't enter into an agreement,

there's no need for him to make any royalty payments, not even interim payments, until the rates have been set, although he will then be required to make back payments, but that won't be until mid-2002 or about three and a half years after the DMCA went into effect.

If a webcaster doesn't agree with us, he has no obligation to participate in these proceedings or even to assume any of the cost of these proceedings. In short, there are many disincentives for webcasters to negotiate with us, and notwithstanding those disincentives we were able to successfully negotiate 26 agreements.

Now, Section 112 specifically says that you may consider rates and terms in voluntary agreements. Section 114 says that you may consider rates and terms in voluntary agreements with comparable types of digital audio transmission services and for comparable circumstances. The webcasters' focus on that comparability language that's in Section 114, not in Section 112, they argue that all licensees are not comparable to those for

whom you must set royalty rates, because some of them are not operational or because they were motivated by special considerations to deal with us.

Well, the facts are that 13 of our licensees are operational, six have not yet commenced operation, and seven have either been acquired or are no longer operational. And we believe that this is very much reflective of the universe of webcasters. Indeed, the record will show that as of the beginning of this year there were about 750 Internet-only webcasters who had signed for the Section 114 license. And of that number, more than 500 were not in operation at that time. The record will show that significant consolidation in the industry is not only inevitable but is already going on, just as it has happened in other industries.

It is also a fact that many of our licensees are very small, some are medium sized, and one is very large. Again, we believe that the record will show that our licensees are very much a cross section of the webcasters for which you must set rates and terms. The industry itself is populated by a few

large webcasters, a number of medium sized webcasters, and many small webcasters.

And, furthermore, when you consider the issue of comparability in this case, consider one other thing as well: The webcasters' case is based on the notion that record labels are interchangeable with music publishers, that sound recordings are interchangeable with musical works, that the Internet is interchangeable with over-the-air radio, and that digital rights are interchangeable with analog rights. Now, I don't believe that they're going to meet their burden of establishing that any of these things satisfies the test of comparability that they themselves advocate.

Now, when you read the webcasters' case, you can't help but to come away with one very definite impression: The only reason these guys are in business is to help us sell records. And it's true that many of our record labels have very good working relationships with many webcasters, including some of those in this proceeding. And we expect that those relationships will continue. But those relationships

typically involve target promotions of particular recordings that fit within our overall business strategies, where we have control over exactly what it is that is being done.

Now, this is very different from what it is involved in this proceeding where a webcaster has the unilateral right without our consent or even our input to pick and choose from any and all of hundreds of thousands of sound recordings and then to transmit those sound recordings over the Internet whenever and however they choose so long as they comply with the requirements of the DMCA.

Now, virtually every commercial operation who uses our recorded music, legitimately or illegitimately, claims that its use is promotional. And I think we would agree that many uses of our music are promotional, at least to some degree. But that does not mean that they have the right to make use of that music by paying us some token amount, whatever is left after they pay all of their other expenses.

Now, as I've explained, we're going to be relying on this case primarily on agreements that the

recording industry associations negotiated and that individual record labels have negotiated. I think what you will see is that in all of these cases the factor of promotion has been taken into account. We have agreements, for example, for music videos. Music videos are created for the primary purpose of promoting the sale of sound recordings, but it doesn't mean that we give companies who want to build their business on those music videos the right to use those videos for free. And we'll be discussing later today, as well as throughout this proceeding, exactly what it is that we received in the marketplace for not only music video agreements but also other types of rights that are analogous to the rights involved in this proceeding.

Let me also just briefly mention our case concerning the business establishment, Section 112, license. Now, you walk into a store, like a Gap, and you may hear music in the background. These services provide that music to the Gap and other stores like them for a fee. Under the law, these services are exempt from paying us a performance royalty, but they

may and must pay us for any copies they make of our recordings in order to provide this service. And certain of that copying is subject to the statutory licensing provisions in Section 112.

And this part of the case I think is complicated somewhat for the fact that the parties do not agree on what Section 112 actually covers. We filed a motion with the Copyright Office asking for clarification and explained what we thought was covered. DMX and AEI are the only two business establishment services in this proceeding, and actually it's only one since AEI is now owned by DMX. They opposed the motion for clarification without saying precisely what it is that they thought was covered. The Office, in its July 16 order, chose not to afford any guidance of precisely what is covered by Section 112. Instead it told the Panel to set rates and terms for everything.

Our position here is the same as it is with the webcasters. For years, record labels have entered into negotiated agreements with DMX, AEI, and other business establishment services. And those

agreements set rates and terms for the copying of our recordings by those services. And we believe that under the willing buyer/willing seller standard, the rates and terms you set for the Section 112 license should be consistent with the rates and terms that we have negotiated in those agreements. And we will be presenting witnesses to describe those agreements. And, indeed, we've put a number of them into the record here as well.

Now, as you know, this is the first proceeding in which a CARP must set rates for the ephemeral recording licenses. However, it's not the first proceeding in which the CARP must set rates for a digital performance right in sound recordings. In 1997, another CARP conducted a proceeding to determine that royalty that certain subscription music services must pay. And these are the services that provide music programming over cable television or DBS, or Direct Broadcast Satellite, systems.

We requested a rate of 41.5 percent, which was the average of what other cable programming services were paying for their copyrighted

programming. The CARP, however, adopted a rate of five percent. And while the Librarian found that the CARP had acted arbitrarily in a number of respects, it increased the rate to only 6.5 percent.

Now, while we respectfully disagree with the decision in the subscription services proceeding, we have tried to respond in several ways that are relevant to this proceeding. First, and perhaps most importantly, we successfully urged Congress to adopt a different standard for setting the webcaster rates. The original standard required the CARP in the subscription services proceeding to set rates and terms that achieved certain statutory objectives in Section 801(b)(1).

And this slide will show what those objectives are. Both the CARP and the Librarian construed those objectives to permit a below market subscription services rate. And that construction of the statute was then affirmed by the D.C. Circuit. And when Congress considered extending compulsory licensing to webcasters, the quid pro quo that we sought was a fair market value standard.

You take a look at who's on the other side of the room here. You have AOL, you have Viacom, who owns MTV, who owns Infinity, who has ownership interest in BET, the Comedy Central, all of whom will be testifying before you here. You have Clear Channel, one of the largest -- the largest broadcaster in the United States here. Our view was that our industry should not have to subsidize the likes of AOL and Viacom and Clear Channel. We should not have to subsidize them with below market rates, and Congress agreed with that. It replaced the Section 801(b)(1) objectives with the willing buyer/willing seller standard.

The Copyright Office has made clear in its July 16 order that that willing buyer/willing seller standard that you must apply is very different from the standard applicable to subscription services. As the Office explained on page 1 of that order, Section 114 contains two separate and distinct standards for setting rates and terms.

Second point to note about the subscription services proceeding is that the CARP in

that proceeding rejected our reliance upon licensees paid by cable networks, and that was what the 41.5 percent was based on. It said that these fees were paid pursuant to agreements that involve different parties, different works, and different rights than the ones that were at issue in that case.

Furthermore, the CARP considered the best benchmark to be a single agreement that three of our companies had entered into with one subscription service, even though we had entered into that agreement at a time when we had no performance right at all. The Librarian said that the agreement was not a good benchmark, primarily because of the fact that it had been negotiated at a time when there was no performance right in sound recordings. Nevertheless, the Librarian used the agreement in setting its rate, and in fact the ultimate rate in that proceeding is very close to the rate that was in the one agreement that was the central focus of that original proceeding.

We learned from that decision and from that proceeding, and we've sought to address points

that were expressed by the CARP and the Librarian in that case. And that's why we are relying here on agreements that involve the same parties, the same works, the same rights that would be involved in the negotiation that you must replicate.

Third point that I want to make about the subscription services proceeding. The Librarian uses a benchmark in that proceeding: The royalty that subscription services paid for musical works, even though the parties had actually paid little attention to musical works before the CARP. The Copyright Office, in its July 18 order, has made clear that you are not required to use that same benchmark here. Rather, you must decide on the basis of the record before you whether it makes sense to use musical works as a benchmark for studying the webcasters' royalty. And it's the burden of the webcasters to establish that musical work rates are an appropriate benchmark.

Again, we have sought to address the points made by the Library and the subscription services proceeding. We believe that the record here will show that musical work fees, and particularly

musical work fees paid by over-the-air broadcasters, is not an appropriate benchmark.

Let me move to the last topic that I wanted to discuss with the Panel here, and that's the rates that we propose and the rates that the webcasters have proposed. The differences between us and the webcasters are not merely theoretical. They lead, as you might suspect, to some very different royalty rates. Now this is evident if you compare our proposed Section 114 rates with the webcasters' proposed rates. And the following slide shows the rates proposed by both parties here.

A couple of things to note. We would afford the webcasters an option. They could either choose from a percent of revenues or a per-performance metric, whichever they chose, presumably would be whatever one gave them the lower royalty. Our percent-of-revenue option is 15 percent of the revenues attributable to the webcasters' transmission of our sound recording, subject to a minimum fee. Webcasters don't have a percent-of-revenue option, even though that's the way the radio stations, on

which Professor Jaffe relies, actually pay their royalties, as a percent of revenues.

Under our per-performance option, the webcaster would pay four-tenths of a cent each time one person listened to one song. For example, if I listen to ten songs on AOL's Spinner, Spinner would owe a royalty of four cents -- ten times 0.04. We have a slightly higher rate for what we call a B-to-B, or business-to-business, service; we also call it a syndicator. This is someone who provides its service to other web sites, rather than directly to consumers and usually charges a fee to that other service running the web site. There would also be a minimum payment of $5,000 if you chose that per-performance option.

The webcasters also have a per-performance rate, but it would apply only to non-music-intensive webcasters. As you can see just by comparing the numbers on the left and the right hand side, their per-performance royalty is approximately one-thirtieth of our per-performance rate. The webcasters' principal rate proposal is based on what they call

aggregate tuning hours. Under that approach, the webcaster would pay 15 one-hundredths of a cent for each hour that someone listens to its service, regardless of how many songs they may listen to during that hour. As you will hear, there can be a very significant difference in the number of recordings per hour, and that ATH approach does not take account of those differences.

The webcasters want every webcast of a radio station within 150 miles to be free. We don't draw any distinctions between whether or not those transmissions are within or outside 150 miles. This is an issue that has its origins in other language in the statute that you'll hear more about as we go through this proceeding.

But going back to my earlier discussion of the Copyright Office's July 16 order, what the webcasters must show here is that the willing buyer and the willing seller would agree to a price of zero for those retransmissions. We don't think that the evidence that you will receive when fairly considered will show that the fair market value of those

retransmissions is zero.

The chart here doesn't include the Section 112 rates. This is somewhat of a moot point since the webcasters say they want a zero Section 112 rate. What we are seeking is a rate that is ten percent of whatever it is that is paid pursuant to the per-performance or the percent-of-revenues rates. During the hearing, we'll talk more about the details of each of these rates proposals.

At this point, what I want to do is show you how the different rate proposals compare to the level of royalties that have actually been negotiated, not only by the Recording Industry Association but also by individual record labels for analogous rights. The individual record labels have entered into a number of deals with new media companies that transmit sound recordings or music videos over the Internet. We have placed 23 such agreements in the record and have sought leave to add an additional 30 agreements that are referred to in testimony of our witnesses. That's all in addition to the 26 RIAA license agreements. We've also included another 30 or so

agreements that a representative of traditional licenses, such as compilations and background music services. So all told, our witnesses will be testifying concerning more than 100 specific licensing agreements involving the use of sound recordings.

At this point, Your Honors, what I would like to discuss more specifically with you the actual rates that are found in those licensing agreements, rates that are in not only the RIAA agreements but in the individual agreements negotiated by our companies. All of that information, as you know, has been marked restricted in this proceeding. I also want to discuss with you information that my friends from the webcasters have marked as confidential and restricted in this proceeding. And that's obviously a discussion that I would very much like to have in public. I cannot, because both sides here have requested confidential treatment of that material. So at this point, I would respectfully request that the only persons to remain in the room are those who, under the protective order, have been cleared to receive restricted information.

CHAIRPERSON VAN LOON: Let me clarify. The other speakers on behalf of the owners and performers will not have restricted parts of their opening presentation?

MR. GARRETT: And once I finish with the restricted portion, Your Honor, I will be done with my closing statement here. I don't think it will take very long, but we could then bring everyone back in at the conclusion of that statement.

CHAIRPERSON VAN LOON: Under the same basis that we announced and talked about earlier, a unanimous agreement of the Panel, we ask all those other than Counsel to step outside very briefly.

MS. LEARY: I would like a point of clarification. Does any of the restricted information contained in Mr. Garrett's statement apply to my clients, Public Radio, in which case I would choose to be here for that portion of his presentation.

CHAIRPERSON VAN LOON: Mr. Garrett?

MR. GARRETT: Well, that raises a difficult question, Your Honor. Obviously, all of the information that we're presenting here we think has

applicability to NPR. The issue of Ms. Leary not having access is one that we've been debating since the beginnings of this proceeding. And, frankly, I thought that we had resolved that issue by agreeing to a certain amendment of the protective order, but that agreement would not allow her to remain while we discuss the material that is about to be presented.

MS. LEARY: I am representing NPR. I am in-house Counsel for NPR, and that is why I cannot see the restricted portions of the proceeding. My question to Mr. Garrett is, is there any -- if there is information that is relevant to my clients that is restricted, I would like for some sort of a notice of what that will be, and then we can act accordingly.

MR. VON KANN: I didn't quite understand. Are you planning in the closed portion to say anything about NPR?

MR. GARRETT: No.

MR. VON KANN: So it's only with respect to the commercial licensees?

MR. GARRETT: Well, I'm only going to be talking, Your Honor, about the specific royalty rates

that have been negotiated by RIAA and its individual record companies, as well as certain financial information that has been submitted by the webcasters. Now, if Ms. Leary wants a concession from me that nothing in those agreements applies to her clients and that all of that information is wholly irrelevant to her case, that's not a concession I'm about to make here. But the issue that you should realize is that from the very start we have discussed with Ms. Leary here what her status in the case should be. She chose not to get outside counsel. She chose to represent NPR in-house. We all agreed to a protective order, including Ms. Leary, that said that those who are in-house, whether they're counsel or non-counsel, would not have access to any restricted information.

Furthermore, after that protective order had been entered, Mr. Rich had come to me, on behalf of Ms. Leary, and asked if I would waive a portion of that order so that her experts would be able to get access to restricted information. I said that I would do so on the condition that that would then end the issue of how we treated Ms. Leary. That condition was

then entered as part of an amendment to the protective order.

MS. LEARY: If I may? I sought from the very beginning to not have to have the restrictions not apply to me as in-house Counsel. It isn't a matter of not choosing to hire outside counsel; it's a matter of cost for an entity as small as Public Broadcasting. We believed it was important for us to be in this proceeding, and I am representing us here today for that very reason.

At the time the confidentiality order was drafted, no one knew what anyone else was going to designate as restricted or confidential. In-house counsel would have had access to confidential documents but not the restricted documents. As it turned out, the RIAA marked all of their case restricted. I only very unwillingly acceded to allow my expert witness access to the restricted material, because it was very clear from five weeks of talking to Mr. Garrett and pointing out how awkward this was going to be that we weren't going to get anywhere without some sort of an accommodation. It is not one

that, by any way, I willingly accepted. It was just the best of a very bad situation.

But I understood that materials that pertained to NPR and Public Radio's case specifically would be available to me. They were all restricted materials that they filed in the proceeding in response to my case I have been provided with. So if there is specific information that this Panel is going to hear with respect to Public Broadcasting, I would submit that is a different situation than what we contemplated, and I think I need to have some idea, you know, kind of a Vaughn Index, if you will, of what this material is going to cover.

MR. GULIN: Ms. Leary, if he covers materials having to do with the 25 webcaster agreements, I guess now 26 webcaster agreements, do you consider that information that has something to do with NPR or Public Radio?

MS. LEARY: If it's applied specifically, Your Honor. If it's not, if it's just part of the case they have already submitted and there is no direct application to Public Radio, then I would

understand that to be governed by the terms of the order we did enter into. So I'm asking, frankly, for a point of clarification here. Is there anything specifically referring to Public --

MR. GULIN: Well, I think he's already indicated he's not specifically going to mention Public Radio, but, again, anything that goes to his benchmark might impact your particular --

MS. LEARY: Yes, we understand that.

MR. GULIN: -- case. So I guess at this point you understand what the agreement was, and you understand that the agreement was that as long as Public Radio's not specifically mentioned, even though what he's about to talk about may impact your case, that you're not entitled to stay. You understood that that was the agreement you entered into.

MS. LEARY: Yes. I'm pleased to say it's not that way in the federal courts, only in CARP proceedings.

MR. VON KANN: Can I raise -- this issue sounds to me like it, a, might come up again with some of the testimony as we go along, and it may merit some

more in-depth discussion. But I sort of hate to delay -- I wonder if we can have an arrangement in which Ms. Leary departs at this moment with the understanding that if we revisit this in some fashion, that portion of the transcript could be given to her so she won't -- it's not like she's forever losing her moment to hear it. And we can then, at an appropriate time when it isn't delaying everything else, come back to this issue if we need to.

MR. GARRETT: That is perfectly acceptable.

MS. LEARY: Thank you, Your Honor.

MR. GARRETT: And I just want to make clear, Your Honor, that what we're doing here is going to be talking about rates that are contained in RIAA agreements and in record label agreements, all of which is already in the record, Your Honor. I'm not talking about anything that isn't already in the record and that hasn't been marked as restricted.

We're also going to be talking about confidential financial information that the other side has presented. I, of course, have no objection to her

listening to the information about the other side here. I'm only concerned those rates.

MR. STEINTHAL: Let us be clear that we have no problem treating Ms. Leary under the protective order so that she would simply be bound by the protective order as if she was outside counsel. Our side of the table has no problem with deeming her the equivalent of outside counsel for purposes of the case.

MR. GULIN: Obviously that side does.

MR. STEINTHAL: Yes.

MS. LEARY: Well, it's acceptable. I think it's important that we move on with this portion, and we get back to the portion of opening, but I appreciate --

MR. GARRETT: I guess my long-term concern about this arrangement is it is at least conceivable that this Panel does not accept your benchmark and that you're going to need to make some other arrangements in terms of a benchmark. And you would not have had access to the information regarding their benchmark, which may conceivably be the benchmark the

Panel adopts. So I'm not sure how you intend to deal with that possibility without outside counsel of an amendment of the existing agreement.

MS. LEARY: Well, the latter would be preferable.

CHAIRPERSON VAN LOON: And it sounds as if the proposal from Judge von Kann works in terms of being able to allow us to move forward quickly today.

MS. LEARY: Absolutely.

CHAIRPERSON VAN LOON: Okay. Thank you. This is the appropriate time then for those who are not part of the legal teams to absent themselves.

(Whereupon, the foregoing matter went off the record at 2:35 p.m. and resumed in Closed Session.)

CHAIRPERSON VAN LOON: Well, it's our understanding that the rest of the afternoon will proceed with the benefit of a full public ear to the proceedings. So we'll turn it over to you. Thanks.

MR. RIMOKH: Thank you, Your Honor. My name is Jacques Rimokh, with the firm of Bingham Dana, and I'm here representing the Association for Independent Music, referred to as AFIM.

The Association for Independent Music is a professional trade association dedicated to the support and promotion of independent music of all genres. Members include hundreds of independent record companies, as well as wholesalers, distributors and retailers. AFIM supports and wholly incorporates the case of RIAA herein, but we believe it was critical to participate in this proceeding, because it is important for the Panel to consider the economics of the hundreds of independent record companies and the substantial impact that the rates established in this proceeding will have on those small businesses and the artists that they foster.

AFIM will be presenting the testimony of

Gary Himmelfarb, who is the President of RAS Records. RAS Records is a typical AFIM member and a typical independent record company. It is operated by a small staff of only five people, including Mr. Himmelfarb. It has modest offices just outside D.C. It generally releases between 12 and 15 albums per year, although as you'll hear in the testimony, last year, due to decreased sales, they could only release eight albums.

Like many of the independent record companies, RAS Records specializes in a particular musical genre. It's genre is reggae music, and it has a catalog of approximately 300 recordings to which it's adding to every year.

Mr. Himmelfarb's testimony will give you a snapshot of the life and existence of an independent record company, but primarily it will establish two points. First, it will demonstrate that the independent record companies are small businesses, like many small businesses, operate on very tight margins. Small increases in costs or decreases in sales revenue can have a substantial impact on their viability as a business. Moreover, for example, the

decrease in sales they may have one year will decrease the amount of music they're able to bring out in the following year.

Second part is many of these independent record companies are dedicated to a genre, much like the highly themed webcasts are going to be. The independent record companies are very concerned that with these highly specific themed channels, a user can now sign onto the Internet and instead of buying CDs from our catalog could simply set his computer to the web site and listen to that instead of that. And that substitution for sales, we would submit, is a substantial factor that we, as a willing seller, if we were a willing seller, would incorporate into our negotiations. Thank you very much.

CHAIRPERSON VAN LOON: Thank you very much.

MR. LEVINE: Good afternoon. My name is Arthur Levine. I'm with the law firm of Finnegan, Henderson, Farabow, Garrett & Dunner. I'm Copyright Counsel to the American Federation of Television and Radio Artists, better known as AFTRA, and I appear

decrease in sales they may have one year will decrease the amount of music they're able to bring out in the following year.

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CHAIRPERSON VAN LOON: Thank you very much.

MR. LEVINE: Good afternoon. My name is Arthur Levine. I'm with the law firm of Finnegan, Henderson, Farabow, Garrett & Dunner. I'm Copyright Counsel to the American Federation of Television and Radio Artists, better known as AFTRA, and I appear

before you today on their behalf. I'm also Copyright Counsel to the American Federation of Musicians of the United States and Canada, AF of M, but in this proceeding, the AF of M will be represented by Patricia Pollach with the law firm of Bredhoff & Kaiser. General Counsel of the AF of M will present an opening statement on behalf of AF of M after I conclude.

AFTRA is a national labor organization representing more than 80,000 performers and newspersons throughout the United States. Fifteen thousand of those members are vocalists on sound recordings, including approximately 4,000 singers who have royalty contracts with record labels and 11,000 singers who are background singers.

During this proceeding, you'll hear a great deal of discussion of the business aspects of the webcasting and recording industries. AFTRA hopes to put a more human face on the proceedings. The monies generated by the webcasting royalties set by this Panel will, in part, to real people, performers, and we hope that that amount will represent

significant income for them at some point in the future.

As you know, for decades, performers have heard their recorded performances performed over radio and television over and over again but have received no compensation from the broadcasters. Because of the powerful lobbying effort of broadcasters, there is no performance right for these sound recordings. At the same time, the composers of music have received significant payments when their music has been broadcast.

When Congress enacted the Digital Performance Right and Sound Recording Act in 1995, it provided for the first U.S. sound recording performance right of any kind. That Act ensured that royalties collected under the Act are shared with the performers on the sound recordings when the sound recordings are digitally performed. Traditional broadcasting continues to be exempt from any payment for performances, even when it's in digital form, because the broadcasters' political power has not diminished over the years.

Put yourself in the position of an artist whose performances are broadcast and broadcast with no payment. They feel exploited. Now, a new stream of income under the Digital Performance Right and Sound Recording Act opens up to them. The question, however, is whether at the end of the day performers will continue to feel as though others are reaping financial benefits from their efforts. Will this new right prove to illusory or will it be a right which provides significant income? Will the royalties set by this Panel result in the level of income to the performer which reflects the value of their artistry?

And in that regard, I suggest that without referring specifically to the numbers in the last chart that Mr. Garrett showed you under the restricted portion of his opening statement, if you take the figure proposed by the webcasters for nine webcasters and multiply that by two and a half percent for non-featured musicians, which AFTRA represents, and divide that by the number of non-featured musicians, you come up with a minuscule number for each non-featured performer, as well as for if you do the same

multiplication at 45 percent for featured performers. It's not a realistic number, in our opinion.

Royalty artists now receive a royalty for the sale or distribution of each sound recording of their performance. The don't receive any fee for making an album. Their contracts with the record companies generally provide for an advance. From that advance, the artists pays all of the production costs of the album, 50 percent of the independent promotion costs, 50 percent of the costs of videos, and 50 to 100 percent of the tour costs. These costs are subtracted from the royalties by the record companies, and this is called recoupment.

Until all of those costs are recouped, the artist doesn't receive any money from the sale of sound recordings. As a result, it usually takes two to three years before even a successful artist receives his or her first royalty check. The license fees that are set by this Panel are not recoupable. This will be real money to performers, and for many royalty artists, these fees will be the only income that they receive from their performances on sound

recordings.

You'll hear in testimony from Greg Hessinger, the National Executive Director of AFTRA, that is a webcaster was forced to create its own sound recording for streaming, the minimum cost for the webcaster to create this recording for transmission would be over $350 for a four and a half minute recording. What this suggests is that the webcasters enjoy a significant benefit under the compulsory license allowing them to webcast.

All that the performers ask is that the rate set by this Panel be such that the performer is compensated fairly. It is, after all, the performers -- the Chet Atkins, Barbara Streisands, Tony Bennetts -- who transform the musical composition into hugely popular recordings. That popularity is what makes them valuable to webcast. Please understand, however, for each Atkins, Streisand or Bennett, there are royalty artists and background singers who do not enjoy anywhere near approaching the financial rewards of those top singers.

You'll hear testimony from Jennifer

Warnes, a professional singer, songwriter, and record producer, who will describe her career as a recording artist and the effort she has put into her career compared to the financial rewards she has received. Also, you'll hear from Kevin Dorsey, who has performed on more than 200 record, and the studio hours he has spent in the production of recordings as a background singer for Michael Jackson, Aretha Franklin, Stevie Wonder, and others.

Both of these performers will urge the Panel to recognize in setting a rate the significant role of the performer in creating the sound recordings that webcasters use in building their professions. Once again, during the course of these hearings, we urge this Panel to keep in mind the fact that it is the genius of the performer upon which the webcasters are establishing their businesses. We simply ask that this artistry be recognized and rewarded. Thank you.

CHAIRPERSON VAN LOON: Thank you very much.

MS. POLACH: Good afternoon, Mr. Chairman and members of the Panel. My name is Patricia

Pollach, and I'm an attorney with the firm of Bredhoff & Kaiser, and that firm, in turn, is General Counsel to the American Federation of Musicians.

The American Federation of Musicians is an international labor organization that represents over 100,000 member professional musicians in the United States and Canada. Our members include many featured recording musicians, those with royalty contracts, and they also include non-featured recording musicians; that is, session musicians and background musicians working in the record industry.

As my colleague, Arthur Levine has said, recording musicians, both featured and non-featured, have an important stake in this proceeding. Congress has mandated that the recording artists must share in the receipts from the webcaster compulsory license. And Congress has said that 45 percent of those receipts must be allocated to featured artists, two and a half percent of those receipts must be allocated to non-featured musicians, and two and a half percent of those receipts must be allocated to non-featured vocalists. Thus, in total, 50 percent of the receipts

from this compulsory license are going to go to performing artists, both featured and non-featured and both vocalists and instrumentalists, or musicians.

You already know you're going to hear voluminous evidence in this proceeding about the business of the webcasters, and you already know you're going to hear voluminous evidence about the business of the record companies. But the basis of the businesses you're going to hear so much about over the next 12 weeks is a special kind of product; it's a work of art. And the AF of M evidence in this proceeding is going to focus on that art and on the artists, and we will show you how the skill and talent and hard work and the creative genius of performing artists are the key components of this work of art, the sound recording.

You will hear from Harold Ray Bradley who will talk about what happens in a recording session. And he's a witness extremely well-situated to explain to you the role played by musicians, not just because he's the International President of American Federation of Musicians and of its Nashville local or

because he's a member of the Board of Governors of the National Academy of Recording Arts and Sciences, but in particular because he's known as the most recorded guitarist in history whose active recording career has spanned over 50 years, since 1946. You may never have heard his name before this proceeding began, but it's almost certain that you've heard him play, because he has participated in hit recordings with many great artists, such as Elvis Presley, Patsy Kline, Willie Nelson, Joan Biaz, Henry Mancini, Connie Francis, Loretta Lynn, Tammy Wynette, just to name a few.

You will hear from Harold Bradley how what happens in the recording session is the transformation of a song or of the underlying song into something entirely new, a new product. The songwriters are fond of saying that it all starts with the song, and their fellow artists/musicians don't disagree with that. That's true, we say, but it doesn't end there.

And the example that we will spend some time with is the example of the song, "Crazy," written by Willie Nelson. He recorded it on a demo, which is common practice, and reports often say that Patsy

Kline didn't much like the demo, and some reports say she didn't much like the song either, but she agreed to record it, and so a recording session was called in 1961.

Seven musicians were called to that recording session, and they sat around and they listened to the demo, and as you will hear, it was true in that case and not uncommon that that was the first exposure they had to the song. They didn't have sheet music before or rehearsals before. They went to the session, they heard the song, and everybody thought that demo had a lot of problems. And Harold will talk about what some of those problems were.

But they sat together in a four-hour session and proceeded to develop the perfect arrangement and the perfect accompaniment to that particular song and then they recorded it. And that recording became a country hit in the '60s and a pop hit in the '60s. In 1997, the amusement park operators named it the number one jukebox hit of all time. And the greatest hits album that it appears on is still a top seller today.

In our evidence, in our direct case, we have provided you with the demo side by side -- the demo is recorded by Willie Nelson -- side by side with the Patsy Kline recording, and you can compare, and you can see the transformation of the song.

Well, as enthusiastic as performers are about their art as art, it is true that it is also a business, and it's got to provide a livelihood to musicians and singers, to the performing artists, if they're going to be able to continue creating. So we want to say in our direct case and give you some insight into how musicians get paid.

The American Federation of Musicians has long been negotiating a standard collective bargaining agreement that governs terms and conditions in the recording industry, and the compensation part of that agreement really has three completely distinct features. Musicians earn scale wages. They compensate them for the time they spend actually in the recording studio, and that scale wage includes pension, contribution, and it includes a health and welfare payment.

A completely different but extremely important facet of the compensation for musicians is something called the Special Payments Fund. It's not a true royalty, but it is a method of providing compensation to musicians that's tied to sales and that provides them some benefit from sales profits. So companies pay in -- signatories companies pay into the Special Payments Fund based on a formula that is tied to sales, and then the Fund distributes that money to musicians based on a formula that is tied to their participation in the industry. It's a critical part of the compensation for an active recording musician, and it follows that if sales fall, then the industry compensation falls in the industry.

Royalty artists also have the benefit of the royalty contracts that they negotiate separately, but as you are going to hear, and you've heard a little bit already, often the level of sales of their product don't generate royalties under those contracts. And if follows, of course, that reduced sales also will harm royalty artists extremely.

What has been missing -- oh, well, and the

third part of the compensation structure is what we call new use or compensation to musicians if a recorded song gets used in another medium later. For example, if a recorded song is used in a movie sometime later, then there's compensation to the musicians who recorded the song.

But the piece that's been missing from this compensation structure, and missing historically, was compensation to musicians and to vocalists for the exploitation of their songs on the radio or other kinds of performances, and Arthur Levine had already talked to you about that. The American Federation of Musicians long thought that this was a terrible injustice and participated in every effort over many, many years to amend the law to provide a performance right in sound recordings.

At the dawn of the Digital Age, the AF of M was right there with AFTRA and with the record companies working hard for the creation of a digital performance right. And in particular, we worked to ensure that the new income stream that derive from this right would in fact be shared with others. And

we have succeeded in that, and as I've explained, 45 percent to the featured artists, two and a half percent to non-featured musicians, and two and a half percent to non-featured vocalists.

Members of the Panel, the AF of M is proud of the union standards that we've negotiated over the course of five decades, but we also know that these standards are modest when compared with the revenue generated by hit recordings. And now that we are in a position of seeing new businesses poised to generate new revenues that are fundamentally based upon our creative work, and as you determine the fair market rate that these new businesses must pay for the use of the sound recordings that derive from our talent, our hard work, and our creativity, I guess we'd like to remind you of some words that were said at the beginning of the hearing. Mr. Chairman, you told us that Learned Hand said that a royalty was a device in the aid of justice. We urge you to remember the artists' stake in this license proceeding and make the license rate you set truly a device in the aid of justice for artists. Thank you.

CHAIRPERSON VAN LOON: Thank you very much. And that concludes, then, the presentation from the copyright owners and performers?

MR. GARRETT: Yes, Your Honor.

CHAIRPERSON VAN LOON: Thank you.

MR. RICH: Good afternoon, Your Honors. My name is Bruce Rich. I and my colleagues from Weil, Gotshal are here representing three groups of interested parties in this proceeding: broadcast streamers, by which we refer to FCC-licensed radio broadcasters who simultaneously stream their over-the-air programming on the Internet; webcasters, that is entities which run Internet-only audio streaming businesses; and background music services, that is business that provide background music primarily to business establishments.

The way we're going to divvy up this afternoon, in trying to keep up with our friends on the other side, we've got five presenters, actually. I'm going to address the Section 114 and Section 112 fee proposals for the broadcast streamers and the webcasters, as well as the analytic structure

underlying those proposals. Bruce Joseph, of Wiley, Rein, will speak to the particular circumstances of FCC-licensed radio broadcast streamers, as they bear on the issues raised by this proceeding. Denise Leary of NPR will outline the case for the public broadcasters. My partner, David Berz, will address the particular Section 112 circumstances of the background music industry, which, as I think you're aware, are exempt from the 114 liability and for which there is a separate fee proposal from the copyright owners. And last but not least, Mr. Steinthal will address the substance of RIAA's direct case.

By way of introduction, I do want to simply say a few words about primarily Mr. Garrett's presentation and more generally the thrust of the RIAA case. RIAA, it's by now clear, will be relying upon a group of licenses which they claim demonstrate what willing buyers and willing sellers would pay for sound recording performing rights in a free marketplace. Now, while superficially attractive, we intend to demonstrate that in reality these agreements do not form reliable benchmarks for establishing the fees at

issue here. As Professor Jaffe will expand on in his testimony, and has dealt with at a general level in his direct testimony, these types of agreements in fact tell us very little about what other willing buyers, specifically our clients, would pay for these rights.

Strictly as a quantitative matter, RIAA has proffered 25, it would like to proffer a 26th agreement, from a universe of some 2,000 streaming web sites -- 25 out of 2,000. Now, many of these remaining 1,775 or so web sites, such as the broadcast streamers, bear little or no resemblance whatsoever to the 25. Others of the 1,900, I should say, and the 75 web sites have affirmatively rejected the very rates and terms reflected in those 25. And all of the remaining group, incidentally, who have put their lot with this compulsory license proceeding have chosen, as they're entitled, to invoke the protections of the compulsory license and arbitration process precisely, precisely to avoid being caught in the copyright vice where to avoid, on the one hand, copyright infringement penalties or, on the other, abandoning

the streaming of music they must pay the monopoly piper the demanded fee.

Moreover, as Mr. Steinthal will elucidate, even looking at these 25 agreements on their face, on examination they're far less than meets the eye. Section 114(f)(2)(b), which I believe has been handed around to the Panel, as I'll further discuss, permits, for sure, it permits this Panel to examine such voluntary license agreements; there's no issue. But it also instructs that such agreements, if they're to be analyzed, must be scrutinized for whether they encompass, quote, "comparable types of digital audio transmission services," unquote, as well as whether such agreements were negotiated in, quote, "comparable circumstances," unquote -- very, very key provisions.

Now especially during the earliest period of experience with a new statute where there is no history of license experience, where, as is the case with nearly all of the 25 licensees, survival till tomorrow, or at least to the next round of financing, is the overarching corporate objective, at a bear minimum caution in adopting license fees agreed to in

such an environment as benchmarks for an entire industry is in order.

In a parallel setting, the Department of Justice, in a recent amendment to the ASCAP consent decree, has disallowed licenses negotiated within a five-year period in a new market from serving as evidence of reasonable license fees in the ASCAP rate court setting. And what does the government do? It cited the fact, which is equally apt in the case of the RIAA 25, that, quote, "Music users are fragmented, inexperienced, lack the resources to invoke rate court proceedings, and are willing to acquiesce to fees requiring payment of a high percentage of their revenue because they have little, if any, revenue," unquote, words that I believe resonate here and that as the record develops will give enormous poise to the weight to be given to the RIAA 25.

Now, turning to my own overview of our own affirmative case, I'd like to start by talking a bit about the statutory framework that governs here, and, again, turning the Panel's attention to Section 114(f)(2)(b), which finds its parallel in the 112

provision in 112(e)(4). And I'd like to begin, first, by asking and talking a bit about why there is a compulsory license here in the first place, something which Mr. Garrett notably elided from his otherwise comprehensive presentation.

Now, as Professor Fisher will testify, as a matter of legislatively history, the new to U.S. copyright law sound recording performing right was enacted principally out of concern that certain emerging means of distributing music enabled by new technology might reduce sales of sound recordings. Principal focus of concern was on downloading; that is, the placing of copies of digital sound recordings on the hard drives of consumers' computers, and on on-demand streaming, the so-called celestial jukebox, which permits the consumer to listen, typically for a fee, to streamed music of his or her choice on demand.

Now, for those kinds of activities, for on-demand streaming or to provide functionality, or functionally similar interactive, as we might call them, services, first the DPRA, in 1995, and then the DMCA, in 1998, compelled the entity desiring to stream

music in one or more of those formats first to obtain licenses from the owners of the sound recording.

Now, these are not, however, the activities involved here, which instead involve what Professor Fisher refers to as ancillary methods of distributing music over the internet, specifically noninteractive, nonsubscription webcast. I might say parenthetically, that it's a given that neither are we concerned here under this compulsory license, focusing on noninteractive, nonsubscription webcasts with video licenses, with jukebox licenses or with a panoply of other licenses negotiated dealing with different copyright rights, in different markets, with different players and not subject to the concerns which animated the compulsory license here.

And the activities we are concerned with, however, pose far less of a threat to the copyright owners than the forms of downloading and on-demand streaming which animated the legislation to begin with. And indeed, as our uncontested evidence will demonstrate, our clients' webcasting activities promise to produce enormous, enormous promotional

benefits to the labels, no differently than over-the-air broadcast radio has done for generations.

Now, admittedly, this new and emerging line of commerce raises a dilemma, which is discussed by Professor Jaffe in his testimony. The clearance of performing rights to stream large numbers of sound recordings entails potentially large transactions, of course, making the concept of a centralized collective, offering, if you will, a form of blanket license an attractive license option. But at the same time such a collective almost by definition enjoys very large market power. The RIAA represents all of the major labels, several hundred independents and its members account for fully 85 percent of all records sales in the United States.

Now in balancing this dilemma, the public policy solution which the Congress reached in the Act, both to facilitate these emerging businesses while constraining the market power resulting from allowing a collective to offer these kinds of blanket licenses, wants to create the compulsory license mechanisms, of Sections 114 and 112.

I should note that it's a little bit ironic and more than a little ironic to hear Mr. Garrett not too subtly suggest during this opening that indeed, there is a concern brought about by compulsory licensing and that is somehow artificially to depress the prices which the monopolists would otherwise extract in the marketplace. With due respect for that argument, I think he's got it completely backwards. The purpose of the compulsory license and indeed, I think, a prior CARP precedent here would indicate that being the case is designed frankly to constrain the possibility that super competitive pricing would be achieved in the market place and if there were any doubt about that one need only look at the legislative history of the Act and the Department of Justice
Anti-Trust Division expressions of point of view about that subject.

Now as I will now get into the statutory license mechanism, indeed, the structure of the governing language has important implications for evaluating both sides of the cases. First, the very

fact that we're dealing with a statutory license, with a licensing mechanism that takes away exclusive license authority from the RIAA's members is itself meaningful.

As Professor Jaffe's testimony elucidates, if Congress had considered it acceptable for a "market rate" to be one set simply by the interaction of RIAA and/or its individual members with our clients, it wouldn't have created the compulsory license. It follows, as Professor Jaffe testifies, that the compulsory license is designed to achieved something other than a simple replication of the license fee experience that would occur in its absence. We sharply and completely disagree with the RIAA proposition to the contrary, namely, that it is scarcely more of a role for this Panel than to determine that, in fact, a series of agreements were reached and that since those agreements were reached in this marketplace, and were "voluntarily entered into" by several third parties, that that basis presumptively becomes the basis on which an entire industry's license agreements were reached.

Again, the statutory license results from a recognition of the market power enjoyed by the RIAA in this instance, market power that but for the anti-trust exemption afforded its statutory license-related activities would raise serious competitive concerns.

Indeed, where no compulsory license protection exists, where the labels have unfettered license authority, for example, with respect to interactive services, it's notable under the statute, this is 114(e) of the statute, that RIAA is explicitly barred from negotiating prices and terms on the industry's behalf, precisely out of the concern -- this is now the Department of Justice's words, of the implications of a "licensing cartel" with the power "to set higher than competitive prices."

Now with that -- those thoughts in mind, let's take a look at the statutory language itself. Section 114(f)(2)(B) provides that the Panel -- may I have another copy? Thank you. Provides that the Panel "shall establish rates and terms that most clearly represent the rates and terms that would have

been negotiated in the market place between a willing buyer and a willing seller."

In reaching this determination the Panel shall base its decision on economic, competitive, and programming information presented by the parties, including "whether the use of the service may substitute for or may promote the sales of phono records" and "the relative roles of the copyright owner and the transmitting entity in the copyrighted work and the service made available to the public with respect to relative creative contribution, technological contribution, capital investment costs and risks." Notably, going on and indicating that in establishing such rates and terms, the Panel may -- not shall -- may consider the rates and terms, as I quoted earlier for comparable types of digital audio transmission services and comparable circumstances under voluntary license agreements.

That this Panel's role is not ministerial, that it is not confined to blessing as market approximating any deals that RIAA might proffer to it is plain, not merely from the public policy and

economic underpinnings of the compulsory license as discussed, but from the foregoing language itself, we would submit.

The Panel shall establish rates and terms that most clearly represent those that "would have been negotiated" not "that have been negotiated" in the marketplace between a "willing buyer and a willing seller." And that determination shall be based on a wide range of information comprehending economic, competitive programming, promotional value and considerations of relative costs, investments and technology and the risk calculus set forth in the statute. Those are all mandatory attributes of what would have happened in a marketplace, taking account of all of those that must go into the determination of what the willing buyer and willing seller in this market would have agreed to. As noted, it's not a coincidence. It's not accidental that the language permits the Panel to consider voluntary agreements. It may do so, but it need not and at that, as noted, it must assess whether those agreements pertain to comparable types of transmission services and were

entered into in comparable circumstances. Nowhere, nowhere does the statutory framework state or imply as RIAA would perhaps otherwise have it, that conclusive weight must be given to such voluntary agreements. Quite instead, the Panel's assigned task is to determine the rates and terms that a willing buyer and seller would have agreed to in a competitive market, a market not characterized by the market power that the RIAA collective brings to bear in its negotiations, a market in which the panoply of economic, competitive, programming, promotional value, cost, risk, and other considerations that the Panel is charged with examining are brought to bear. Now this competitive market test is precisely the standard, precisely the standard, that has been adopted in the conceptually-related ASCAP and BMI rate courts, charged with determining reasonable fees, that is, fees that approximate fees that would be established in a free market setting.

There, as well, while evidence of prior agreements has been of some relevance to the musical works fee setting process, it's been far from

conclusive on its face. In affirming the trial court's rejection of such a proffer by ASCAP and the cable television setting, then Chief Judge Newman wrote the following for the Second Circuit, "the opportunity of users of music rights to resort to the rate court whenever they apprehend that ASCAP's market power may subject them to unreasonably high fees would have little meaning if the court were obliged to set a reasonable fee solely or even primarily on the basis of the fees ASCAP has successfully obtained from other users."

Now despite RIAA's urging, nothing has changed with respect to the foregoing tools of analysis since 114(f) was amended. The issue here was before and certainly is now that the determination of what a competitive market rate would be with respect to the services engaged in by our various clients, that is the nub of the concept of willing buyer/willing seller. It is the nub of the issue here and it is the nature of the market that one needs to look at and that market needs to be not a market characterized by the existence of market power

manifested in the agreements we've seen, but rather, that hypothetical competitive market which necessitates this entire proceeding.

And as I indicated, there can be no question from the face of the statute that in making that determination all of the factors which the Panel is required to look at, the shall part of the statute, must come into the analysis and the Copyright Office, most recently, in this case has affirmed that indeed that list of factors is not exclusive and that the Panel is free to take evidence on an array of other factors that may well inform the Panel as to the nature of what a willing buyer and willing seller rate would constitute.

A few words about the prior CARP proceeding that Mr. Garrett spoke to. Mr. Garrett suggested that that CARP explicitly adopted a below market standard. I would suggest that a proper reading of the decisions in that case indicates that when the Panel reached for the analogous music performing right, musical work, performing right in that case, it indicated that that rate itself framed

the upper and lower bounds of reasonableness, of what the market would bear, and indeed perhaps giving the tilt there to the 801 factors suggested that an outcome at the lower range of the potential rates suggested by the musical works performing right was appropriate.

The upper range of rates then would have been about 8 percent because at that time there was one final deal in place and that was a deal in which DMX had agreed to pay BMI 4 percent as a final royalty. There was an issue there because there were nonfinal royalties in place with ASCAP and so there was supposition as to what the final rates might be. So you had a potential upper bound rate of about 8 percent in that case. You had a final result as Mr. Garrett indicated of about 6.5 percent following a Panel's prior determination that the rate would be 5 percent. A correct reading of that case is not that the 8 percent rate would have been supra market. Indeed, quite to the contrary it would have been the upper range of what the -- everybody felt would be reasonable.

Now the reason I harp on this a bit is that just last week there was a decision rendered by Judge Stanton in Federal District Court in New York in a case involving not DMX which had been the benchmark standard setter for the prior CARP, but by a competitive named Music Choice who also had been a party to that prior CARP proceeding and Judge Stanton determined that the very 4 percent fee which had formed the basis for the prior CARP should not be, should not form the basis, was not a proper competitive market benchmark for fee setting for Music Choice, although Music Choice was a direct and is a direct competitive in that market. Judge Stanton instead set a fee for Music Choice at 1.75 percent of music for BMI. This is now Music Choice's revenues. And when one thinks about that against the backdrop of the prior CARP proceeding, it's more than enlightening because again, as we read the prior CARP proceeding and I think the most reasonable reading, you now have a basis for fee setting there which has been effectively cut in half in the BMI rate court setting and suggesting that a rate which was itself determined

to be market approximating upper bound 8 percent, would not be a rate, in fact, that would be more closer to half of that amount if that proceeding and that record evidence were updated to the present moment.

Now for the reasons already noted, the limited license experienced to date within the new market for sound recording performing rights, as well as the fact that those licenses are the produce of noncompetitive market conditions and reflect license circumstances as Mr. Steinthal will address that simply aren't comparable to those of our clients, that combination means that that experience forms no basis for the fee determination here.

We're left to find a benchmark that's more suitable. And that benchmark is for all of the reasons that Professor Jaffee illuminates in his testimony, the broadcast radio industries performing rights payments for the musical works embedded in and integrally associated with the sound recordings in this case. This is an important concept, Your Honors. This is not a work that is plucked out of thin air and

having no relationship whatsoever to what we're about in this proceeding. Every time a sound recording is performed, there are two performances occurring. There is a sound recording performance itself, a subportion of which is before this Panel, and there is at the same moment, and integrally associated with it the performance of the underlying musical work. They're inextricably linked with one another. And so there is -- even at its root there is a core and fundamental rationale in the absence of probative evidence of fair market value, competitive market value here. There's a compelling need to look elsewhere and there is a compelling logic, we would suggest in looking to the very corresponding musical work performing right which is embedded in and inextricably associated with the very same sound recordings of performing rights which here are before this Panel.

And there are a number of positive attributes associated with looking at that experience and tweaking it and shaping it and doing the necessary to it to make it comparable for our purposes because

in contrast to the limited and nonrepresentative license experienced to date in regard to the sound recording performing right, the musical work performing right has been negotiated over many, many decades. Its fee structure is in place not for a couple of dozen licensees, but with respect to thousands of broadcasters. The fees themselves don't represent a trivial amount of commerce at this point, but rather amount to hundreds of millions of dollars literally, annually in license fee payments. And again, simply to emphasize the two performing rights are totally complementary. The one generally can't be performed without the other.

Now Mr. Garrett, in his opening simply suggested that our case is predicated on the flawed notion that the music publishing business and the record business are in his words interchangeable, I think he said. We make no such contention, nor need we sustain any such contention to prevail with respect to our model. We make the much more modest assertion that in searching for admittedly imperfect surrogates of a free market, couldn't agree more, Judge Van Loon,

about the difficulty and intangible quality of the process in which we're engaged. It's a given. But nevertheless, we are required to search for analogs that work and that make sense. What we are saying is that there is logic, there is rationale and indeed there is history here for looking to the next best, we would assert, market option, given the failure of the 25 agreements we believe at the end of this process to stand up to analysis and that is a comparison of the music performing right and the sound recording performing right. The demand sound is the same for both, has nothing to do with the underlying economics of the music publishing business versus the record business. These are inextricably combined. You need both in order to perform the very same sound recordings.

Now given these attributes, it's not surprising that the one prior CARP charge with setting the Section 114 rights that for the subscription digital cable audio services utilized this very benchmark. As I mentioned, they are using it as a ceiling on the sound recording performing right. And

I mentioned to you what Judge Stanton recently did. I won't repeat it. I will simply also note that quite recently the Canadian Copyright Board adopted the very same broadcast radio musical work performing right fee as the benchmark. Indeed, it said that the very fee payable there should be identical to govern the Canadian sound recording performing right payable under Canadian copyright law. This is not made up out of whole cloth. There is a strong rationale for it.

Now how do we, very briefly, how do we construct our model? Again, I'm not going to do this in detail because it's in Professor Jaffe. He first examined the royalties that over the air radio broadcasters paid to the three music performing rights organizations. That's ASCAP, BMI and SESAC. He determined that the music characteristics of over the air radio are similar and in many cases identical to the product that the webcasters stream over the internet. And that on that basis he further considered the economic relationship that the music performing right should bear to the sound recording performing right and derived the conclusion which is

in his testimony and consistent with that of the prior CARP that the right in issue in this proceeding should command a lesser performance royalty than the musical work performance right.

Now the fee basis for this proposal is quite straight forward. What Professor Jaffe did was to find a metric that could be used across media and what he did was to take a fee experience and data reflecting what radio broadcasters have paid and translated that into a fee per listener number. And as the testimony indicates, that on a per listener hour, the basis is a fee which is 22 hundredths of a cent -- .22 cents per listener hour.

Now because we face circumstances in which in some cases webcasters do not intensively use music, they have programming formats that use music quite occasionally and other circumstances in which webcasters may determine as they are legally entitled to to secure some of their music performing rights requirements in direct transactions with the copyright owners. We and Professor Jaffe felt it appropriate to construct alternative fee structures that both

accommodate that reality with respect to a subset of the webcasters, namely those who don't use music intensively who would otherwise be taxed unfairly based on the analysis which is predicated on a music intensive format from blanket licensing in the ASCAP BMI world and also again to incent as a matter of competitive, desirable competitive outcome, to incent those webcasters who wish to do so. We use Comedy Central as an example in our papers, to secure in the marketplace the rights directly and so as an alternative of pricing methodology and approach constructed as described in Professor Jaffe's testimony and in his appendix, there is developed in the alternative a per listener song fee, as opposed to per listener hour, something that's driven by the volume of sound recordings actually utilized by the webcaster, or in the alternative, something that we've styled a segmented listener hour fee which covers solely that percentage of listener hours as contained compensable of sound recordings.

Having made those baseline benchmarks, Professor Jaffe proceeded to make the necessary

adjustments to take account of the relative economic relationship between the basic music performing right as to the musical works and the sound recording of performing right and in determining that the sound recording royalty should be lower, should be lower than the ASCAP royalty, this at Professor Jaffe's testimony beginning at page 35, Professor Jaffe sets forth a series of reasons and criteria that lead to the conclusion and other openers today are going to focus on several of these which include the enormous promotional value of the public performances of sound recordings, far greater in magnitude than is the case with respect to the owners of the musical works copyrights. And equally important, Professor Jaffee cites to as the statute instructs the Panel to do, the enormous technological investments, the significant capital contributions, the great risk of not recouping investments with reasonable returns faced by streaming broadcasters.

At bottom, Professor Jaffe concludes, based on what the record evidence will show that it is the licensees who incur costs relative to revenues

collected with respect to services that are disproportionately higher than anything sustained by or occasioned to the record industry. Having in his analysis going through two methodologies for determining in a quantifying sense possible promotional discounts, looking at the international experience which Mr. Kempton does in his testimony and at the U.S. experience, the conclusion derives from that analysis which again is in the papers that the overall value of the performance of sound recordings, pardon me, the implied sound recording royalty, in other words, the rate to be established herein is about 52 percent of the estimate musical works royalty that's the U.S. experience, the experience from international is slightly in a band of 40 to 70 percent. Professor Jaffe takes the most conservative discount, if you will, 30 percent from the listener hour and per listener song fees, to derive a bottom line of a blanket license fee of 15 one hundredths of a cent per listener hour and a listener song model at 1.04 or 14 thousandths of a listener song, per listener song as the basic fee driving this

proceeding.

A couple of quick words and I'll end on ephemeral copies. Mr. Garrett misstates our client's position in ascribing a zero value or suggesting that we ascribe a zero value to ephemeral copies. That's not the burden and the gist of our testimony.

What we do say is that the value of the ephemeral right is inextricably tied into and reflected in the value of the performance right itself. As Professor Zittrain's testimony demonstrates, the only function performed by ephemeral copies is to facilitate and effectuate public performances. As Professor Jaffe testifies, there is no value in such copes separate or distinct from the value of the performances they effectuate. In other words, the performances generate the economic value. That's not tantamount to saying there is no value to the ephemeral copy, but rather in examining here the value of the performing right, it already embraces without allocation whatever value might separately be ascribable to the ephemeral copy.

This suggests that while the Panel might

be free to allocate some portion of the monetary formulas that we suggest if you were to adopt it, to the ephemeral right, the total value, nonetheless, should not exceed the value of the performing right because of this basic economic recognition which is it is the performing right that drives the value. It isn't the separate and distinct value because there is none in the ephemeral copies. The approach we urge the Panel to adopt is to assess a single package royalty, if you will, equal to our 114 fee proposal, but if the Panel were to determine to set a separate rate, then the sum of that royalty and the right of public performance should not exceed the reasonable fee proposal we make with respect to the performing right. And secondly, if there is a separate rate to be assessed, the portion ascribable to the ephemeral copy, given its very limited and ancillary role, should be relatively small in relation to what that performing right is.

With that, I'll speed the dais.

CHAIRPERSON VAN LOON: Mr. Rich, I see one of your colleagues on his feet already.

MR. JOSEPH: I try not to waste any time, given the clock moving with us. Actually, if you'll bear with me -- by the way, my name is Bruce Joseph. I'm with the Washington, D.C. law firm of Wiley, Rein & Fielding. We represent Clear Channel Communications, Salem Communications and the NRB, the National Religious Broadcasters Music License Committee. I will be speaking to you about a very special type of streaming at issue here, that is the simultaneous streaming by radio broadcasters of their broadcast programming.

And before I begin, I'm going to ask my colleague, Karyn Ablin to pass out two exhibits that contain precisely the only restricted words that I would utter if this were a closed proceeding.

Rather than making everybody get up and leave, I am going to simply comment that Your Honors may turn to Exhibit 1 and Exhibit 2, but not peeking now. They come in contact and we don't want to ruin it, so I will tell you that you may turn to --

MR. VON KANN: May I have the envelope please?

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In the matter of:	Docket No. 2000-9
Digital Performance Right in Sound Recording and Ephemeral Recording	CARP DTRA 1 & 2

CARP Hearing Room
LM-414
Library of Congress
Madison Building
101 Independence Ave, SE
Washington, D.C.

Monday
July 30, 2001

The above-entitled matter came on for hearing, pursuant to notice, at 1:00 p.m.

BEFORE

THE HONORABLE ERIC E. VAN LOON Chairman
THE HONORABLE JEFFREY S. GULIN Chairman
THE HONORABLE CURTIS E. von KANN Arbitrator

MR. JOSEPH: I try not to waste any time, given the clock moving with us. Actually, if you'll bear with me -- by the way, my name is Bruce Joseph. I'm with the Washington, D.C. law firm of Wiley, Rein & Fielding. We represent Clear Channel Communications, Salem Communications and the NRB, the National Religious Broadcasters Music License Committee. I will be speaking to you about a very special type of streaming at issue here, that is the simultaneous streaming by radio broadcasters of their broadcast programming.

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MR. VON KANN: May I have the envelope please?

(Laughter.)

MR. JOSEPH: To Exhibit 1 and Exhibit 2 at a suitable time. Nobody else will need to leave. I'm afraid I won't be able to tell you all exactly what I'm saying or what they're seeing at that time, but that's how I think we can proceed and spare everybody the need to get up.

I'm going to discuss several key points with respect to the simultaneous streaming of radio broadcast programming. Again, that's what I'm talking about.

First, Congress has long recognized the unique symbiotic relationship between radio broadcasters and record companies. Consistently rejecting record company efforts to obtain a public performance right. And when it finally granted a limited right in 1995, Congress specifically exempted radio broadcasts because of the promotional value of those broadcasts to the recording industry and by that I include both the record companies and the performing arts.

Second, I'll show how Congress got that

part right. The record will demonstrate that radio broadcasts have enormous promotional value to record companies and artists and the record companies spend millions upon millions of dollars to cause radio stations to play their records.

Now radio streams on the internet, of course, contain exactly the same content and go primarily, the evidence will show, to the same audience as radio streams over the air. The only difference is whether you're listening on a computer or whether you're listening on a radio.

Third, I'll discuss the relevance of the radiobroadcast market and what I've just spoken about, the promotional value to this proceeding. The longstanding relationship between record companies and radio stations provides compelling evidence of what a wiling buyer would pay a willing seller for the inclusion of sound recordings and radio broadcast streams in a free, open and competitive market.

Fourth, I'll take a brief look at the evidence related to radio broadcast streams provided by RIAA. RIAA offers no evidence of any deals with

broadcasters. None. So when Mr. Garrett argues that RIAA's case is fundamentally based on deals with the same licensees and speaks of thousands of channels of highly themed music, that has nothing to do with the simultaneously streaming by radio stations of their broadcasts.

Finally, I'll discuss the relative balance of costs, risks and benefits which weigh overwhelming in this case in favor of the rates and terms proposed by the broadcasters and the webcasters.

Let's turn to congressional recognition of the importance of radio broadcast to the record industry. We should start with Congress because after all, it's Congress that has the power to enact legislation granting copyrights. I might add as an aside that RIAA simply has it wrong when they call the rights at issue here fundamental rights. The power has been granted under the Constitution to Congress to grant copyrights, to create copyrights to serve the public interest by creating an incentive. There is no God given right to collect for public performances.

Ever since a limited copyright and sound

recordings was recognized in 1972, Congress has repeatedly rejected the grant of a general public performance right. Even in 1995, when the limited public performance right for subscription and interactive digital transmissions was finally adopted, Congress again reiterated its view that there should be no sound recording performance right applicable to radio broadcasts.

Now Mr. Levine disparaged this fact as simply the political influence of the broadcasters. Nonsense. RIAA and the recording industry takes a backseat to nobody when it comes to political influence. This was not about political influence. The House and Senate reports when the 1995 Act was passed both specifically say why and I might add they did so with marked understatement. And I quote, "the sale of many sound recordings and the careers of many performers have benefitted considerably from airplay and other promotional activities provided by radio broadcasting."

Accordingly, Congress decided in 1995 that it would do nothing, and again I quote, "to change or

jeopardize the mutually beneficial economic relationship between the recording and the traditional broadcasting industries."

Congress went even further. They recognized the radio broadcasts might be digitally retransmitted within the same market as in over the air broadcasts. Thus, it expressly exempted even third party digital retransmissions within 150 miles of the broadcast transmitter. That's the 150 mile issue that Mr. Garrett referred to earlier and there will be more about that as the case develops.

Now Congress amended the Sound Recording Performance Act of 1998 with the Digital Millennium Copyright Act, but nothing in the 1998 Act upset these key determinations and these key points.

So what does this all mean? The legislative history bespeaks a congressional determination that zero is, in fact, a reasonable payment by radio broadcasters for the performance of sound recordings in their broadcasts, taking into account all of the relevant values, including the promotional value.

That determination adhered to for decades and recently reaffirmed should provide the starting point for Your Honors. Granted, it's not the ending point. Congress has given the recording industry a chance to come here to show why that rate that prevails in radio should not prevail on the internet. In other words, to show that internet streaming differs in material ways from broadcasting and that those differences justify their proposed rate.

They haven't made, in fact, they haven't even attempted that showing. To the contrary, our evidence will show that broadcasting and streaming, especially streaming of broadcast programming are extraordinarily similar and that a fee close to that congressionally determined zero rate for over the air radio is a fair approximation of what a willing buyer would pay a lone seller on the internet.

Let's look for a minute, and actually it may take more than a minute, at the promotional value of radio to the recording industry. The evidence will show extraordinary promotional value. To see this, you will need to look no further than the recording

industry in the record companies own conduct. First, the record industry's own data will show that companies spend millions upon millions of dollars to independent promoters in order to induce radio stations to play their records. They spend additional millions advertising for the radio industry and undertaking other promotional activities to cause airplay. Record companies supply thousands upon thousands of free CDs to radio stations. They don't have to do this. They could charge, but they don't.

Every single radio witness will confirm that record company representatives aggressively seek play on radio stations because they view radio play as critical to the success of their records. Every one of the radio witnesses.

We'll also provide direct evidence from our direct case of evidence of promotional value. Michael Fine, a recognized expert on the industry and on what motivates consumer purchases of records will testify and this is worth quoting: "It's a universal truth in the music industry and radio airplay of music has a powerful promotional effect on the sale of sound

recordings. The more a song is played on the radio, the greater the sales of recordings that include that song."

He also says, "Radio airplay is clearly an overwhelmingly the most significant driver in motivating music consumers to make album purchasing decisions." He generates data from his business that shows that 67 percent of all music consumers stated that what they hear on radio most influences them when it come to buying music and specifically, he found that 27 percent identified heard on the radio as the factor that most influenced a specific record purchase which is more than twice the next most commonly mentioned factor.

We'll offer survey conducted by Professor Michael Mazis confirming that more than half of the respondents said that listening to AM or FM radio motivated their last music purchase.

How is that general information about radio promotion relevant to a proceeding about the internet? Well, you've now heard several times that you're charged with determining what a willing buyer

would pay a willing seller in an open and competitive market for the rights to perform sound recordings. Those rights, of course, can't be examined in a vacuum. They must be considered in light of all of the benefits of performances to the record companies and the performing artists. They are, after all, the putative sellers in that market.

The free and competitive market that exists today in connection with broadcast programming is directly relevant. The programming of course is the same. Dr. Mazis' study also confirms that most of the listeners are the same. Now even though there's no sound recording performance right in that market, there are other rights that the record companies could exploit as "willing sellers" if they believe that it was in their economic interest to do so.

So let's look at what that market looks like. Well, millions upon millions of dollars spent to convince radio stations to play their music, record companies have the right to charge for CDs, but they don't. They give millions of dollars worth of free CDs to radio stations, other words, in the closest

competitive market that exists radio doesn't pay the record companies. The record companies spend huge sums of money to induce radio stations to make performances.

Now all of that should be enough to make you stop and ask in a true, freely competitive market on the internet, who would be paying whom?

Jim Donahoe, a witness from Clear Channel says it well in his testimony, "record companies eagerly pursue the opportunity to have their recordings played on our stations. In an open, competitive market, they would pay us for the privilege of having their recordings played. Thus, it seems perverse that radio stations should have to pay the record companies for doing what they constantly beg and pester us to do."

Let's look at RIAA's proposed fee model. RIAA, I have already said, has no negotiated licenses with broadcasters. None of the 25, not even the 26th, they proffer, zero. Now that's out of 1,557 broadcasters who have filed notices saying that they are going to use the Section 114 license.

MR. VON KANN: What was that figure again?

MR. JOSEPH: One thousand five hundred fifty-seven. I'm not making that number up. It's not mine. It actually comes from RIAA's direct case, page 4, footnote 2 of Steve Marks' testimony.

That fact in itself should cast serious doubt on RIAA's case as to broadcasters. Remember, Mr. Garrett stressed that he was trying to present evidence of exactly the same licensees. They don't. He also speaks of licenses granting rights to thousands of channels. That has nothing to do with the radio broadcaster who is streaming its broadcast programming on one channel.

Now even beyond that, only 2 of RIAA's 25 agreements even have anything to do with third party retransmitters of radio broadcasts. And remember, those aren't even the members of the industry that Congress referred to as having a long-standing mutually beneficial relationship. These are third party retransmitters.

Let's briefly look at those two deals. This is where the exhibit will come in handy.

According to data produced by RIAA on April 27th, one of the services, a small company, a small web company called Cyberaxis, has paid the amount reflected on Exhibit 1, thus far under its RIAA license as of April 27th.

Do you all have that? Okay. Now you'll hear much more about the other licensee in a little while from Mr. Steinthal. For now, I'll note only that the relationship between the deals allocated rate for broadcast retransmissions and RIAA's requested rate is instructive and just to give you a moment to look at that allocated rate versus RIAA's requested rate, you should look at Exhibit 2.

Now without saying whether it's higher or lower, because I don't want to tip anybody's hands, but even under RIAA's theory of the case which for all of the reasons we've discussed is simply not correct, and for all of the reasons Mr. Rich discussed and for all of the reasons Mr. Steinfeld will discuss it's not correct, the fee you see on Exhibit 2 logically would serve as the most RIAA even under its own theory could seek for radio broadcast transmissions.

I'm going to digress for a moment and pick up two other quick points before turning to my last one.

First, and actually Bruce Rich touched on these so I won't spend a lot of time with them, any fee model must accommodate different radio broadcasting formats and they must also accommodate direct licenses. A lot of radio, as you know, is not all music. There is certainly no basis for RIAA to collect a fee for talk shows, news and sports formatted programs with essentially no feature performances of music. There are also other mixed formats. Joe Davis of Salem Communications will tell you about religious formatted stations represented by the NRBMLC. Those stations perform relatively few sound recordings. They actually sell blocks of time to ministries who have teaching and preaching programs in relatively few programs and those programs -- to those performances of music typically don't drive the station's revenue. Any fee model that's ultimately set needs to take these format differences into account and charge streamers proportionally for their

use of sound recordings. The proposal of the broadcasters and webcasters meets that criterion.

The fee structure should also encourage direct licensing, that is, as Bruce Rich mentioned, directly negotiated deals between individual copyright owners and streamers. Congress has directed you, after all, to look at competitive market models. You should be sure that by setting a fee in this proceeding, you don't destroy the incentive for a competitive market to develop. And the only way to permit that is to develop a fee structure that doesn't require the streamer to pay twice if it goes out and acquires a direct licensee. The broadcaster/webcaster proposal includes this feature. As far as I can tell from reading it, RIAA's proposal at this point, does not.

Finally, a few comments about relative contribution cost and risk, particularly with respect to radio broadcasters who are trying to stream on the internet. The testimony of the radio broadcasters you'll hear makes several things clear. Radio station websites generally, and streaming through those

websites in particular, are simply extensions of the radio broadcasting business. They exist to promote the radio business and to enhance the listeners' relationship with the station. Thus, record companies and artists are benefitted in two ways. First, they receive the direct promotional benefits of play during the stream. Second, to the extent streaming strengthens the commitment of the listeners to the radio station, it enhances the promotional value of the performances on the radio station. The witnesses will also tell you that streaming is extremely expensive. Bandwidth and technology costs are enormous. The radio witnesses will testify as to the huge costs and risks that they're bearing to try to get in to the streaming business. No radio broadcaster is now making money streaming. Stephen Fisher of Entercom will testify no streaming radio station has been able to convince advertisers to pay more for over the air ads streamed over the internet. And because most streaming radio stations can't even deliver 1,000 simultaneous listeners over the internet, at present there's simply no market to sell

with respect to advertise for internet streaming.

Dan Halyburton of Susquehanna will testify, all of Susquehanna stations streaming operations are running at a loss. To date, Susquehanna stations have covered no revenues from streaming and Infinity, the second largest radio group in the country doesn't stream, simply because it doesn't believe there's a sensible business model to support the activity.

Now these are the views of some of the largest players in the industry. Think of how difficult it is for the smaller players.

The royalty rates set in this proceeding will have a profound impact on whether there ever will be a radio streaming business on the internet.

Now against these huge documented costs and risks incurred by the radio broadcast streamers, and also the benefits and the lack of benefits to the radio broadcast streamers, there's no evidence that streaming adds any cost or risk to the record companies or the record industry. The record industry witnesses will talk about huge costs and risks of

producing records, but those costs and risks are all sunk. They relate to the production and sale of records and are more than compensated for by revenues by existing lines of business, most notably, record sales. Any revenues from streaming are pure gravy.

The record companies' talk of risk in this context must be hugely discounted. It's not a risk from streaming and as you will see, the marginal cost of streaming to the recording industry is zero. In addition to bearing no costs, of course, we've already talked about the promotional burden, I'm sorry, excuse me, the promotional benefit. So in sum, when you take the relative costs, the relative risks and the relative benefits, those factors will weigh decidedly in favor of the broadcast streamers in this proceeding.

For all of these reasons, we submit that the property royalty for radio broadcast streaming is the fee proposed by the broadcasters and webcasters.

Thank you for your attention.

CHAIRPERSON VAN LOON: Thank you.

MR. GULIN: Thank you, Mr. Joseph, before

you sit down I just have one quick question for you to clarify what you mean by a broadcaster streamer is a broadcaster that streams simultaneously, retransmits simultaneously its own signal with no changes, doesn't insert ads?

MR. JOSEPH: The relevant proceeding before this Panel relate to the sound recordings and it's the simultaneous streaming of the sound recordings. There may be ad insertions.

MR. GULIN: But other than that's it's just their own signal that's been retransmitted?

MR. JOSEPH: It's their own.

CHAIRPERSON VAN LOON: Thank you. Ms. Leary.

MS. LEARY: Good afternoon. I'm Denise Leary and I'm representing 407 public radio stations as well as NPR itself. I'm going to take a little stretch and put up -- thank you. I have one visual aid to assist the Panel and it is the same as Table 1 in our experts report.

(Pause.)

Your task, as you've been over abundantly

reminded today, is to determine what the reasonable fees are that should be paid by public radio to the RIAA for the right to publicly perform sound recordings through a digital medium such as the internet.

In this proceeding we represent many of the educational, noncommercial public radio stations which are licensed by the Federal Communications Commission. I want to note parenthetically that public television is not a party in this case so the Panel has before it just the task of setting rates for public radio.

We have more than, as I mentioned, 400 public radio stations all of which are qualified to receive federal funding from the Corporation for Public Broadcasting. There are statutory requirements that a public radio station must meet to qualify as noncommercial and educational. You will hear testimony that they must be owned or operated by a public agency or a nonprofit, private foundation or corporation or association or a municipality. They may transmit only noncommercial programming for

educational purposes. Approximately two-thirds of the stations that we represent are licensed to colleges and universities. Their educational mission is clear. The balance are licensed to nonprofits that hold the license and community or municipalities that have set up a broadcasting station in an area that's not served generally by commercial broadcasting.

Our mission in public radio is to provide culturally enriching educational programming which is generally unavailable in any other medium. This is true whether you look at --

MR. VON KANN: What these guys are doing is not culturally enriching? I'm surprised to hear that.

(Laughter.)

MS. LEARY: I make no comment. This is true whether one looks at either webcast programming or broadcast programming. Our programming is highly produced and generally forms into one of three categories: news, information or cultural, each of them designed to enhance the listener's life. We were created by Congress to accomplish two significant

purposes, to provide unique and diverse programming and to harness technology to advance education. We've done that through the broadcast medium and we are now doing that through the internet for the very same purposes. We view the internet as a powerful new medium and a necessary one for us to reach more diverse audiences in unserved areas. It is simply another part of the mandate of public broadcasting.

The unique quality of our programming on the web and on the air is reflected in the hundreds of awards that have been bestowed. Public radio has won radio broadcasting's equivalent of the Triple Crown. We've won the DuPont Columbia, the Peabody and the Pope Awards for many of our programs. More recently, in December of this past year NPR's cultural programming division heard on a number of the stations that are before you in this proceeding received the National Medal of Arts. It's a congressionally-established medal and NPR was the first media organization ever to win this award. This is the division within NPR and the aspect of public radio programming that makes the most intensive use of

music. Many, many, many of the hours that we distribute over the web and on air have absolutely no music in them, save for theme music which is generally commissioned by public radio and is owned by it.

The award that I mentioned honors those who make an outstanding contribution to the excellence, growth and support and availability of the arts in the United States. More recently, we have begun to achieve recognition for our webcasting program as well. The availability of high quality programming is very much the mission of public radio and that is why the internet is the necessary tool. As you will hear later on in the testimony of our witnesses, the number of web listeners that we have is extremely small by comparison with our broadcast audience. This is a factor we take into account in adjusting our benchmark fees.

Programming placed on the individual websites of public radio stations as well as national public radio and Minnesota Public Radio is for all intents and purposes the very same programming that is broadcast by each station or in the case of National

Public Radio, distributed to our stations for their broadcast.

When financially possible, additional printed resources and visual aids are added to the webcast to enhance the educational value. There is very, very little web based only programming available on public broadcasting. We too are for a large part streamers. We hold substantial archives of our news and information programming for listeners to come back and listen to a second time.

The financial value that the recording industry accords to its license is a great overstatement of its intrinsic value as one of the many components we used to put together public radio programming. They seek a significant fee and their direct case sets forth business models and economic analysis that we would submit is vastly overpriced as to all webcasters, broadcasters and particularly to public radio. There is, indeed, no license agreement with any noncommercial, educational entity in the RIAA's case before you, nor is there any factoring of the missions and economics of public radio which, as

a recent Panel noted in deciding the fees to be paid for musical works by public broadcasters on 1/18 should be taken into account. The Panel stated that commercial and noncommercial broadcasters do, in fact, operate under different economic models and one should not be surprised that these models yield somewhat different results, including differences in fair market rates. This is simply absent from the RIAA's case.

Section 114, as we've discussed numerous times today, directs you to consider which rates most clearly represent what we've been negotiating in the market between a willing seller and a willing buyer and that you are to look to the economic competitive and programming information presented in this proceeding, including whether our web programming substitutes for or promotes the sales of records or if it interferes with or enhances the recording industry's stream of revenue. We would submit that these factors all favor public broadcasting.

You must also consider the relative degree of creative contribution that public radio adds to

what the copyright owners of the sound recordings have indeed created: our technological additions to enhance the quality of the sound, the visual and printed materials that we usually put up in conjunction with our webcasting and the investment and costs and the risks that public radio takes on in relationship to the copyright owners. We would note again that the motion brought by the RIAA for proper statutory standard to apply to this case, the Copyright Office noted that the arbitrators should consider the two factors I just enumerated, but they should not limit your deliberations to these factors alone.

Last, Section 114 directs you to consider the rates and terms for comparable digital audio transmissions and comparable circumstances for voluntary license agreements negotiated. It is again our position that there is no such comparable license submitted in the RIAA's case.

There is also the direction of Section 802(c) of the Copyright Act which states that arbitration panels considering these matters shall act

on the basis of a fully documented written record, prior decisions of the CRT, prior copyright arbitration panel determinations and rulings by the Librarian of Congress. Given the limited jurisprudence in this realm of sound recordings, we believe that a recent CARP decision provides the best benchmark for determining the rate you should apply here.

We submit that musical works fees which are paid by public broadcasters to ASCAP, SESAC and BMI with proper adjustments are the fees that should be considered by this Panel. The only other recent decision regarding public performance of sound recordings by the digital subscription services with the Librarian's determination in 1998. In that proceeding the fees paid for the underlying musical works by the digital services were used as a starting point. The Librarian ruled that the musical work fees constituted the upper limit or outer boundary, if you will, of the reasonable rate for that proceeding. We submit that little has changed in the ensuing three years that would suggest that sound recordings are any

more valuable than the musical works which they embody. Moreover, in July of 1998, another Panel in a well-reasoned opinion authored by Judge Gulin, determined that public broadcasters should pay for the public performance of musical works in the broadcast medium and we take that as our starting work.

I'm just going to go quickly through our model.

(Pause.)

This is Table 1. It's the first exhibit to our expert witnesses' testimony and you have it before you. And at the risk of giving the rest of you eye strain, I apologize.

CHAIRPERSON VAN LOON: Placed closest to opposing counsel.

MS. LEARY: What we did was we took the rights that were paid for the musical works in the CARP Panel. The CARP Panel had before it just the ASCAP and BMI portions of the total performing rights fees. We had negotiated an agreement with SESAC which is the third programming rights society. And that was a total fee for television and radio. There was no

bifurcated fee in that particular proceeding.

What we did was we added a 3 percent increment to account for SESAC share of the total repertory of musical works, compositions and that gave us 103 percent and applying that to the BMI and the ASCAP fee, we reached a fee of $5,606,000. We then had to decide how much should be allocated to public television of that total fee and how much to public radio. And what we did was we looked at the program revenues over the prior 3 years for public radio and public television expenses. I'm sorry, I said revenues and I meant to say expenses. And we determined what the estimated public radio fee would be, a hypothetical fee for broadcasting ASCAP, BMI and SESAC. We then took that as the hypothetical fee for sound recordings, since we consider them equivalent and we added an additional figure to account for the fact that classical music is in the public domain and therefore it is typically not, music in the public domain is not licensed by the performing rights society by definition. So we added another $800,000 for that and we got an estimated public radio fee for

broadcasting sound recordings. What we then did is take a look at the insignificant audience that we have on the web which is about 1.2 percent of the broadcast audience that we have and we came up with a fee for all of public radio of $24,000. This was based on a survey that public radio conducted among its stations including those that were webcasting, those that may webcast some time in the future and those that have decided against not doing it. And that is the fee that we submit is the appropriate one here.

I certainly want to note that on the revenue side public radio stations do operate quite differently from anyone else in this proceeding, again, something the RIAA has not taken into account. Our sources of revenue can be very unpredictable and reductions from any one source can have devastating consequences both throughout the system level and at the station level. Any one component that is valued more highly than another will have a direct affect on our ability to use that component in our programming.

Funding sources do include federal and State and local government budgets, university/college

budgets, contributions from individuals, typically during those difficult-to-like pledge drives and underwriting from financial institutions and businesses.

I don't want to repeat what has been gone over so well by my colleagues. We did not plan our arguments together. We're running the clock and I want to save some time. But I would say that as to the comments on broadcast streaming certainly do apply to National Public Radio and its public radio stations. We have a completely different model that we think you must consider and consider that if you place it too highly we will go back to stripping music out of our programming. We did that for some period of time until we negotiated music licenses with ASCAP, SESAC and BMI because at the time they clearly had a right for digital transmissions. We would go back to that model if this CARP sets the fee too high.

Thank you for your time and attention.

CHAIRPERSON VAN LOON: Thank you.

MR. BERZ: Mr. Chairman, gentlemen, my name is David Berz, I'm a member of Weil, Gotshal &

Manges and I'm here on behalf of AEI Music Net, Inc. and DMX Music, Inc., two companies that were merged and are now wholly-owned subsidiaries of DMX AEI Music, Inc. and that merger occurred in May of this year.

MR. VON KANN: That was after these direct cases were filed?

MR. BERZ: Correct.

MR. VON KANN: I see.

MR. BERZ: Just by way of clarification, since much of this proceeding, most of it covers the period when they were separate entities and because they continue to operate as separate, but wholly-owned subsidiaries, we don't see any particular need to change any of the submissions that we've made to date.

MR. GULIN: Just for the record, what is the merged company called?

MR. BERZ: It's called DMX AEI Music, Inc. and that merger occurred on or about May 18th of this year.

AEI and DMX differ in their circumstances from other users of copyrighted works that you will

hear from in this proceeding in at least two important, but related ways that I want to address today.

First, as you have heard, AEI and DMX are what we generally refer to as background music services. We deliver demographically targeted music to business establishments for use solely within those business establishments and under strictly controlled license terms that ensure that the sound recordings delivered to these businesses never have a second life. For example, consumers don't initiate a background music listening experience. Instead, they hear music which has been specifically selected for the merchants which AEI and DMX serve. Because the music played by background music service clients is intended to be part of an overall shopping or dining experience, the perception of this music is different than it would be when people are delivered music in their homes or work places by webcasters or broadcasters for that matter.

Moreover, because the acoustics in stores and restaurants where background music is used are

different than the acoustics in a consumer's home, even the format, for example, of a programming may differ from the format used by other services. For instance, often our clients deliver monaural music rather than stereo.

I use that by way of example to simply say that many of the concerns with which this proceeding is concerned and will address with respect to other participants simply do not apply to AEI and DMX.

Second, because AEI and DMX deliver content to business establishments rather than directly to consumers, they enjoy an exemption from the obligation to pay copyright owners represented in this proceeding a royalty for the right to make public performances of their sound recordings. As a result, AEI and DMX are concerned with only a limited portion of this proceeding, that portion which fixes the rate, terms and conditions for the statutory license to make ephemeral copies of sound recordings under Section 112(e) of the statute.

AEI and DMX are here to ensure that those rates and terms are reasonable and that the rates do

not eviscerate the overriding congressional intent in granting the background music services, the business establishment exemption. We believe that this is exactly what would happen if the royalty rates proposed by the RIAA were to be adopted.

Now let me give you a brief overview of our case and I do mean brief. In setting a reasonable rate in terms for the making of ephemeral copies for background music services, the Panel is tasked by Section 112 with considering several important factors including whether the use of the service substitutes for or promotes the sales of copyrighted works and the relative roles of the copyright owners and the service providers in making the service available to the public. Each of these factors will be addressed by the testimony of three of our five witnesses. These three witnesses are executives of AEI and DMX. Their testimony will establish four major points. First, the ephemeral copies with AEI and DMX are making are temporary copies which facilitate the types of transmission for which the background music services enjoy an exemption from paying any copyright

royalties. In this regard, these ephemeral copies are never sold. They are used solely to facilitate performances which are exempt from copyright obligation. They are made in the normal course of the operation of the equipment used to transmit the sound recording to the business establishment. Moreover, neither AEI nor DMX derive any revenue directly from these ephemeral copies. The ephemeral copies have absolutely no independently exploitable commercial value.

Finally, the ephemeral copies made provide benefits to the copyright owners such as enabling additional security measures or increasing the quality of sound.

Second, the background music services will demonstrate that they employ a variety of methods to promote, as I indicated, rather than displace the sale of sound recordings by the record labels. Some of these methods include directly financing various promotional efforts on behalf of the labels, investing in technology that facilitates consumer purchases of records and CDs and developing program and marketing

approaches to aid the recording industry in developing and expanding the very markets for their business.

Third, the background music services also employ various technologies and programming measures in accordance with Section 112 of the Act to limit the risk that any ephemeral copies made to facilitate exempt performances somehow make it into the marketplace and dilute the market value of copyrighted work. These measures include the use of encryption as well as other security measures which we will discuss; cross fading tracks to make illicit copying difficult and quite frankly unattractive; and complying with the sound recording performance complements requirements.

Fourth and finally, with respect to the relative roles, risks and investment of the background music services vis-a-vis the copyright owners, the background music services have made a variety of investments in their services which have had the effect of promoting copyright owners businesses and enhancing their traditional streams of revenue. Some of these investments include developing new technologies which provide additional security and

facilitate purchases by consumers and programming content delivered to business establishment so as to provide better exposure of artists and target particular market segments.

Now as you will learn AEI's and DMX's contemplated business plans include continuing to employ new technologies which require the making of ephemeral copies in order to deliver content to business establishments more efficiently and securely. We submit that if a disproportionately high royalty rate is established for the making of these ephemeral copies, AEI and DMX may be forced to use older, less efficient means of distributing content to business establishment. This would benefit neither the copyright owners, the background music services, or the business establishment that the background music services serve.

Now all of these factors in our view argue for setting a flat, annual rate that is modest in relation to other music right fees. In making these arguments, we will rely on the testimony of two highly distinguished experts in economics and intellectual

property law. Professors Jaffe and Fisher, who Mr. Rich discussed, have stated in their written testimony and will explain further when they testify before you, that because the right to make ephemeral copies is unquestionably subsidiary to the right to make the performance in the first place, only a very small share of the overall value of the performance can be ascribed to the right to make an ephemeral copy.

In the case of the background music services which are exempt from the obligation to make payments for the public performance of sound recordings, the Panel must therefore be particularly careful, as I indicated earlier, not to undo Congress's intention in granting the performanc exemption by assigning an unduly high royalty rate for the right to make ephemeral copies.

Now gentlemen, the RIAA has proposed that our clients pay 10 percent of their gross revenues per year subject to a $50,000 per year per company minimum fee for the right to make ephemeral copies. Simply stated, there is no credible support for this demand. Neither the background music service licenses

negotiated with individual record labels, nor the agreements negotiated with webcasters submitted into evidence by the RIAA support its position. Without naming names, the background music service licenses offered as benchmarks by the RIAA set rates at between 16 and 15 percent of gross revenues attributable to the individual, to the use of individual members' sound recordings, less appropriate deductions in their complicated agreements that we'll discuss in the course of these proceedings.

These licenses also grant the licensees a variety of rights far in excess of the right merely to make ephemeral copies to facilitate exempt performances. These agreements provide absolutely no justification whatsoever for the demand that the background music services pay, 10 percent of their entire gross revenues for the right to make ephemeral copies to facilitate delivery of their services to business establishments.

As you have already heard from Mr. Rich and you will hear from Mr. Steinthal, the webcaster agreements which will be offered into evidence by the

RIAA to justify their public programance royalty demands from the webcasters and broadcasters are inconsistent in our view with the appropriate willing buyer, willing seller standard. But they also demonstrate how unreasonable the RIAA demands are with respect to fees for ephemeral recordings. Each and every one of the 25 or so webcaster agreements which contain a provision setting forth a separate fee for ephemeral copies set the royalty rate for the ephemeral copies at a fraction of the rate being charged for the programance itself. In fact, some of the webcaster agreements already set flat rates for the making of ephemeral copies which are lower than the rate proposed by our clients in this proceeding.

Moreover, the RIAA's proposal with respect to AEI and DMX is entirely inconsistent even with the rate the RIAA itself has proposed for the making of ephemeral copies by the webcasters and the broadcasters. Although the RIAA proposes to charge the eligible nonsubscription services 10 percent of the royalty rate, it proposes to charge our clients the background music services a full 10 percent of

their gross revenues for making of similar ephemeral copies.

Given these circumstances and after you have heard the direct testimony of our clients and experts and the cross examination of the industry witnesses, we believe it will become clear that the rate proposed by the RIAA is not one which under the appropriate standard a willing buyer or seller would accept in the marketplace and certainly not a rate that this Panel should adopt.

At the conclusion of this proceeding, we will ask the Panel to set a flat royalty rate of no more than $25,000 per year per company for the making of ephemeral copies to facilitate the delivery of background music services to business establishments. After you have heard the evidence, we are confident that you will find that this rate is reasonable in light of the existing marketplace agreements, the promotional benefits the background music services offer the recording industry and the relative roles as the statute reads, contributions, costs and risks of the background music industry.

Gentlemen, I look forward to presenting our case to you. Thank you.

CHAIRPERSON VAN LOON: Thank you, Mr. Berz. Mr. Steinthal?

MR. STEINTHAL: Can we have about a 5 minute break while we deal with the charts based on a conversation we had earlier?

CHAIRPERSON VAN LOON: Let's be in our seats and ready to go by 5.

(Off the record.)

MR. STEINTHAL: Good afternoon, Your Honors.

CHAIRPERSON VAN LOON: Good evening.

MR. STEINTHAL: I now know why baseball pitchers are notoriously crazy as they have to sit in the bullpen for hours and hours and hours until they get a chance to play.

I have the dubious task of finishing up after those several hours. I know everyone wants to move on and I'll try to be brief, but I do have a fair amount to cover.

The focus of my remarks will be on the

RIAA's case, its significant weaknesses both in concept and as a matter of evidence. I will try not to trod again over paths covered by my co-counsel, but inevitably there may be some overlap at times.

Let me initially comment on the importance, not of the direct case, but of the rebuttal case. I'm going to ask you to be patient as odd as that sounds. CARP cases are rather bizarre from a litigation standpoint. The written direct cases which we have to prepare without any discovery and without any indication of what the RIAA's case would be, confined to a large extent the evidence we may put before you in the direct phase of these proceedings. We have since had an opportunity to analyze and pick apart the RIAA's case in manners that I'll discuss in a moment, but procedurally, there is much evidence and testimony that we may be unable to give you in the direct phase of the case that I urge your indulgence to wait for in the rebuttal phase.

Now on to the RIAA's case. First the flaws and the conceptual basis and then I will turn to the flaws in the evidentiary part of the RIAA's case.

The gist of the RIAA's case as you've heard from everybody today is essentially this. They say you must be guided in setting the rate by the 25, now 26 deals that the RIAA succeeded in signing with webcasters. But the governing statutory standard simply cannot fairly be so construed. As Mr. Rich explained, it is important to separate the shall language from the wood language and the may language in the governing statutory standard. And without going over that in any detail, I'm just going to pin a couple of things and explain where the RIAA's case fails.

Of course, the statute says the Panel shall seek to determine the rate that will be set in a hypothetical willing buyer/willing seller marketplace which the evidence and the precedence will demonstrate is one equivalent to the rate that would eventuate in a freely competitive marketplace. And the statute then goes on to say that the Panel shall base its decision on economic, competitive and programming information of the nature that the statute specifies regarding mandated consideration of the

promotional value of the webcasters' activities versus any substitution effects or displacement effects flowing therefrom. And it mandates their consideration of the relative costs, risks and investments associated with the transmission services involved and their use of copyrighted works.

Finally, and very much in contradistinction, the statute distinguishes from these mandatory considerations by saying that the Panel also may consider the rates and terms under voluntary license agreements only provided, as I'll get to in some detail they are for comparable types of transmission services and under comparable circumstances.

With these provisions of the statute in mind, it is apparent that the RIAA conceptual presentation goes off the trolley in the following several respects. First, it ignores the direction to determine rates that would prevail in a hypothetical competitive marketplace in favor of one that replicates the extremely limited universe of deals that the RIAA actually did. I just want to underscore

something that Mr. Rich said. If all you are required to do is set a rate by rubber stamping the deals actually secured by the RIAA, there would be no reason for this proceeding at all and we could all go home right now, but that's not what the statute requires.

Second, the RIAA case conceptually goes off the trolley in failing meaningfully to take into consideration as the statute mandates the various quote economic, competitive and programming information, unquote, applicable to the parties. In fact, the RIAA does not dispute at all that the broadcasters and webcasters promote rather than displace record sales as Mr. Joseph so eloquently talked about in his opening.

And there is no evidence that our clients in terms of what they do cause substitution or displacement. This is not a case about Napster. This is not a case about downloading. This is a case about webcasting and any evidence that you will see is that there is no evidence of substitution or displacement to concern you and where they go off the trolley is they never really engage on the mandated inquiry with

respect to promotional value versus substitution and displacement.

Next, insofar as the statute requires the Panel to consider the relative costs, risks and investments of the parties in relation to the services that are here at issue, the RIAA entirely ignores this critical comparison in favor of a totally phony construct relating to the differences between -- as I was saying, the RIAA fails to consider the relative costs and risks factor in the proper way by comparing the costs and risks of the labels to the costs and risks of the webcasters in favor of a phony construct they come up with which is a comparison between their costs and risks and the costs and risks of the music publishing business. But the statute doesn't require such a comparison. It requires that you compare the evidence of the costs, risks, investments and the like of our clients and the RIAA and its members in relation to what? In relation to the webcasting business and the webcasting business is use of sound recordings. They don't engage on that at all. The testimony that you will hear will be about all the

costs and risks significant and substantial as they are across the entire webcaster group and that incrementally there's virtually zero cost and risk associated with the sound recordings utilized in this medium, not in some other medium, but in this medium.

You can hear all the stuff in the world about what it costs to sell and distribute sound recordings, physical CDs in the marketplace, and how much more it costs the sound recording owners to do what they do than the publishers pay to do what they do. It's totally irrelevant to the inquiry under the statute.

Finally, and most importantly, the RIAA analytical framework goes off the trolley in two significant effects as it relates to the wording of the statute in relation to the Panel's obligation to consider actual voluntary license agreements, secured by the RIAA.

First off, the language plainly is permissive, not mandatory, a distinction apparently lost in the RIAA.

Second, the Panel may consider such

agreements only under conditions where the prior agreements are with comparable transmission services and under comparable circumstances. Two conditions that Mr. Garrett alluded to, but when you hear the evidence, it is clear that the RIAA has never taken into consideration in preparing its model.

As I will turn to in a moment, the evidence in fact will demonstrate that the Panel has ample basis to be suspect about whether the various deals secured by the RIAA meet either of those two conditions.

Finally, on the conceptual framework, the RIAA is left with its experts, Misters Nagle and Yerman, to advance RIAA's pricing model based on the handful of deals struck by the RIAA.

The Nagle approach, which would permit a monopolist supplier like the RIAA to set a profit-maximizing monopolistic rate, plainly is entitled to no credence in this proceeding. For how could a fee designed to replicate a hypothetical competitive market be based on a plainly monopolistic pricing structure?

Mr. Yerman, meanwhile, would apply the thoroughly inapplicable construct for assessing damages in a patent infringement case to the instant non-infringement situation. His analysis is noteworthy, however, because he validates the view expressed by the broadcaster and webcaster experts that the royalty paid in this case must be a reasonable one.

He also expresses the view that fees should be set at a level that would permit webcasters to obtain a profit, in which case he actually conflicts with Mr. Nagle.

Enough of the flaws in the conceptual framework. Now the gloves come off, and I can turn to the RIAA's evidence, as it were, what it does and does not reflect. There is no question it does reflect that 25, now 26 as of about ten days ago, companies signed agreements with the RIAA covering their rights to stream sound recordings over the Internet under section 114 of the DMCA.

But before getting to the specifics of what those 25 agreements do and do not reflect, let's

pause over one astonishing statistic that has been alluded to before. The evidence will demonstrate that fully 1,700-plus separate services filed notices with the Copyright Office of their desire to avail themselves of the statutory license under section 114, covering some 2,282 website URLs. That stat comes from one of the RIAA witnesses, I think it's Mr. Marks' statement. Many of these are for webcasting services under common ownership. But even with that, the figure is staggering.

Now against this huge universe of services, potentially availing themselves of the statutory license for which this panel will set a rate, a paltry 25, one percent, have reached a voluntary license agreement with the RIAA.

These 25 webcaster agreements the RIAA says should speak for the market as a whole. But we submit to you that the rejection of the RIAA proposal by the predominant massive services speaks much more loudly than the very few that executed licenses with the RIAA. It is far more telling that more than 2,000 potential licensees rejected the RIAA profit rate than

it is that 25 took it. You will hear from dozens of broadcasters and webcasters as to why they rejected the RIAA proposal.

Let's go back now to the 25 license agreements relied upon so pervasively by the RIAA. What do they show or not show, as the case may be? It is true that most of the 25 agreements are at rates on their face that would either start at the per performance rate or the percentage of revenue rate proposed by the RIAA in this case or escalate to that rate by the end of the term. That is the case in fact as it relates to almost all the 25 RIAA licensees, most of which are companies that never streamed, companies that have since gone out of business, or companies so small that no one has ever heard of them, except for one licensee that we have all heard of, Yahoo.

Who are these guys, you ask, the RIAA's 25 licensees?

MR. VON KANN: Who are these guys?

MR. STEINTHAL: That's a good question. Who are these guys? I defy most of the people in this

room going through the list of one through 25 to say in all candor that they have heard of more than one other than the last. Here they are, presented in alphabetical order, and color-coded to indicate those companies that are now out of the streaming business, those that are in black, those that never streamed, notwithstanding their RIAA license in red, and those of any size that are streaming today.

Without meaning to insult anyone, I suspect that unless you are as tied to this case as our staff is, most of these companies, if not all other than the last, you have never heard of.

Now while 24 of the 25 existing or defunct companies on this list may have agreed to rates approaching those of the RIAA's proposal, one did not. But I can't say in open court that licensee's name or that licensee's rate, or even give a range of how much different that rate is compared to what the RIAA seeks in this case. Why? Because it is a state secret to the RIAA.

Indeed, it was a condition of that licensee's deal that it could not participate in any

manner in this CARP, and that it could not cooperate with any party opposing the RIAA in this CARP. Only today, on the verge of the argument, literally ten minutes before openings, did we hear from the RIAA that they had capitulated on a motion we had made to lift his gag order from that licensee's agreement. A lot of good it did us in preparing for today, since by virtue of that clause that they fought us in months of motion practice on, they denied us access and until now, you the possibility of hearing from that licensee.

Isn't it interesting? The RIAA comes to you with a model premised on a handful of so-called willing buyer-willing seller transactions. There is only one licensee of that handful of any meaningful size or import in the webcasting industry. As to that licensee, we know the rate is different than that which RIAA claims is suggested by their willing buyer-willing seller proposal. If I wanted to clear the courtroom, which I don't, I could tell you who it is and just what fraction of the RIAA asked-for rate is reflected by their deal. But I think you already know

that.

But the RIAA has not wanted us or you, never mind the public, to hear about why it is that that licensee's rate is what it is. Mind you, that licensee's rate, while much different than the RIAA's requested rate, is hardly a competitive market or desirable rate to the webcasters and broadcasters.

I will discuss this further in a few moments, but please don't take my comments as suggesting that that licensee's deal reflects a fair or appropriate rate for everybody else. The evidence will show that it too exceeds by a long shot the appropriate outcome in this case.

Obviously you will not hear from us on our direct case about such circumstances since we were denied every and any opportunity to learn anything about it. But we hope that by the time rebuttal rolls around, we will have some more information for you on those issues.

Now how significant was the silencing of this licensee to the RIAA's model? As much as I hate to use the word again, staggeringly so. Take a look

at the next chart.

Obviously we have redacted out the amounts paid by each of the licensees. We have even redacted out the name or names in the pie chart itself. But the chart is incredibly clear about how significant one licensee is to the RIAA model. One licensee has paid 65 percent of the royalties they have collected pursuant to the statutory licenses they have done.

It is also interesting that 21 percent were done by companies that are no longer streaming. They are defunct. They are out of the business. The evidence will show that part of the reasons they are out of the business was the weight of carrying the RIAA license that they had to pay.

That leaves 14 percent of all their collections from the remainder of those companies that are still active in streaming.

What a travesty of justice it would be were an industry-wide statutory rate to be set at the rates agreed to by 24 nondescript companies out of the thousands of potential licensees, whose collective resume indicates that their aggregate fees paid to the

RIAA across all 24 of them were only one-half of the fees paid by the one licensee we weren't allowed to talk to, and that fully 60 percent of the fees paid by this group of 24 licensees were from licensees that could not survive economically.

This leads me to the more general secretive and troublesome modus operandi of the RIAA with respect to these handful of agreements upon which they would premise an industry-wide rate. This is troublesome in particular because the statute says that this panel may consider prior voluntary license agreements only where they are with comparable services that entered into those agreements under comparable circumstances.

The Panel and we can only know whether the 25 licensees are comparable services that entered into those agreements under comparable circumstances to those of the great unwashed, the thousands that did not execute RIAA licenses, if we know all about those services and the circumstances that led them and motivated them to enter into the agreements they signed with the RIAA. But the RIAA made sure that

knowledge about those services and their circumstances would not be freely available to the broadcasters and webcasters.

Each agreement upon which the RIAA relies provides for a one-way confidentiality provision that allowed the RIAA to present the agreements as evidence in this CARP proceeding specifically, while silencing the licensee from having any communications with any third parties about the terms and conditions of their RIAA licenses.

The result was on April 11th, RIAA presented its direct case, relying on its agreements with the 25 licensees, claiming they constituted the best evidence of a generally applicable marketplace rate. RIAA in so doing presented testimony essentially from one person, Steven Marks, the RIAA's lead negotiator for the proposition that these 25 agreements reflected a willing buyer, willing seller standard that is generally applicable to all the thousands of broadcasters and webcasters that filed notices to avail themselves of the statutory license.

Astonishingly, Mr. Marks in his testimony

speaks not only for the RIAA as to the willing seller's perspective, but he also purports to speak, albeit entirely on a hearsay basis, for various webcasters that entered into the RIAA licenses as to their perspectives and motivations.

This modus operandi of the RIAA is particularly disturbing in a proceeding like this where there is no subpoena power and no third party discovery. The RIAA essentially stacked the deck with a proposed willing buyer willing seller standard under circumstances where the Panel has been presented with testimony only from those on one side of that equation, the seller.

We had to make a motion to the Copyright Office seeking the RIAA to waive the confidentiality provisions I talked about, or in the alternative, to strike the prior voluntary licenses upon which RIAA relies just to be able to give those licensees a comfort level that they could speak with us without being in violation of their RIAA agreements.

We made the motion. The RIAA ultimately capitulated as to all except the one up there, which

as I said, they capitulated on today. But it has since balked about the manner in which we may provide assurances to the licensees that they are free to speak with us.

Imagine the following situation. People sign these agreements with confidentiality clauses that say they can't talk to anybody. That is what they know. We can't go talk to them. Make a motion. We finally get the ability to go talk to them. Then the RIAA says you can't show them the order saying that it is okay to talk to us. They made a motion to redact the order which we were going to give to the licensees so we could give them a comfort level it's okay to talk to us.

Worse than all of that is the confluence of all the circumstances. It took us until just a few weeks ago to get the resolution of the motion which would give us even the possibility of talking to these 25 licensees.

Of course by then, the fact is that many of these licensees are defunct. Of course we have to overcome the reluctance of third parties to come

forward where there is no subpoena power to compel them.

The reality is that it is extremely difficult, and certainly impossible on our direct case, for us to present evidence specifically from these 25 licensees. That being said, we will be able to demonstrate to this panel that there are fundamental bases upon which to be skeptical about whether many or even all of the prior licenses upon which the RIAA seeks to rely were with "comparable" licensees who are under "comparable" circumstances. I will talk about this a little bit more in a few minutes.

One has to wonder though fundamentally if all these deals are truly reflective of a free willing buyer, willing seller marketplace, why has the RIAA gone to every length to prevent us and you from hearing from these licensees? If it is truly willing buyers, why did they go to all those lengths to shut them up?

Now moving past the troublesome efforts of the RIAA to silence the licensees, what do the 25

agreements reflect? As you will hear from Professor Jaffe, these agreements may in fact be between willing buyers and willing sellers, but they are not agreements indicative of a freely competitive marketplace rate.

I'm going to go through a few examples to dramatize this situation. Take the following example. Suppose you are a passenger on a plane that crashes in the desert. You go days without water. You come upon a limited source of water. Surely, you will be willing to pay an amount well in excess of the normal marketplace rate for water. The amount you pay is a willing buyer, willing seller transaction. There's no question about it. But not under freely competitive market circumstances.

Very funny, yes? We think that much of your proposal, I might say.

MS. ROSEN: I bet.

MR. STEINTHAL: Surely the buyer's circumstances in this example, which would motivate him willingly to pay lots more than would be paid in a freely competitive market, are different from those

of the general public. Surely no one seriously would suggest that the amount paid by that willing buyer to that willing seller is indicative of the reasonable rate for all consumers of water.

Now let's take a less dramatic example. Hopefully it won't cause any laughter. Suppose you are late for a plane and you come to a 50 cent toll on the way to the airport. Suppose further that there is a huge line at the toll, virtually ensuring you are going to miss your plane. Your circumstances are such that if presented with the opportunity to pay multiples more than 50 cents, even 30 times more, to use a multiple that comes to mind, you would gladly pay that rate to skip the line and enable you to catch the plane. The 15 dollars, 30 times greater than the 50 cent rate, would be a willing buyer, willing seller rate, but not under freely competitive circumstances.

Now let's get even closer to home. Suppose you are an Internet music service that has features which the RIAA has told you are "interactive" and which would make you ineligible for the statutory license, and thus, infringing. Then suppose the RIAA

says to you, if you tinker with your service a little bit and you pay me X, we will treat you as non-interactive, and thus eligible for the statutory license at that X rate.

Surely, the motivation and circumstances of that webcaster, threatened with infringement litigation unless it pays the rate, cannot fairly be deemed comparable to the vast preponderance of webcasters which have no allegedly interactive features. Yet the RIAA, without disclosing such circumstances or motivations to you in its direct case, would inappropriately urge this panel to rely on agreements secured under precisely these types of circumstances in setting a rate for all broadcasters and webcasters, irrespective of their very different circumstances and motivations.

There are other examples which because of the nature of these proceedings, I urge you to be patient to hear about. I assure you, however, that there will be significant evidence about the motivations and circumstances surrounding the 25 license agreements upon which RIAA relies that will

make you very skeptical about whether their circumstances were comparable to the circumstances of the great unwashed that have not executed RIAA license agreements.

MR. GULIN: I am sorry to interrupt. When you just mentioned what if there was a threat against the webcasters that you may have some interactive elements and perhaps if we work something out, you won't have those interactive elements. Are you speculating now that this is something that could have happened? Or are you telling us that that is in the evidence you are going to be presenting?

MR. STEINTHAL: That is going to be evidence I am going to give you.

The examples I recently ran through of varying circumstances among different buyers, different "willing buyers," reflect but one set of reasons to be skeptical about the RIAA's approach in seeking to set an industry-wide fee based on agreements with a mere 25 out of over 2,000 potential broadcaster and webcaster licensees. But it is not even necessary to demonstrate such special and unique

circumstances in order to demonstrate the unfairness of the RIAA's self-selected approach.

The economic evidence will reflect that in any marketplace, there will be a range of willing buyers, a range of willing buyer prices. Sometimes it is called a distribution curve. As the jargon goes, some people are willing to pay more than the free market price for a product, and some are unwilling to purchase a product unless the price is lowered below that rate.

What the RIAA has chosen to do is what in the jargon is price discriminate. We didn't have time to get a chart on this, so I just drew one up.

This is your normal distribution curve in an economic analysis. The price is going to be set at the bell number, where most of the people buying products are going to pay for a product. Sure, there are going to be some people that have certain circumstances, usually a lack of time, where they might go to a store and not care that they are paying higher than what the normal sales price is for a product. But for the most part, the product price is

going to be driven by where the normal distribution is. There are going to be some people that at that price are going to be unwilling to buy.

So what has the RIAA done? The picked off 25 people up here out of 2,000. They have taken the people willing, for whatever their circumstances and motivations, willing to pay a price. They are now saying that because I got the top part of the distribution curve, it is fair and appropriate to saddle everybody with that. That flies in the face of normal economics 101. You can't do it, especially in a situation where you are dealing with an entity like the RIAA that has huge marketplace power.

One more thing I should mention before moving on. The interactivity example in the question from Judge Gulin brings to mind the fact that several label executives will be testifying about non-statutory license deals, including for interactive music on demand service, music video streaming services and the like. Mr. Garrett went through that whole array of different kinds of licenses that you are going to hear about.

We are truly baffled as to why the RIAA is going down that road. Plainly, these are circumstances in which the licensee must secure a voluntary license with the label, lest it be at risk of copyright infringement. The lack of a compulsory license alternative, imperfect as that alternative may be, puts the webcaster at far more risk in the absence of a negotiated agreement.

Hence, the label, when we are dealing with non-statutory licenses, has much enhanced bargaining leverage and can be expected to drive a much higher than compulsory rate. The non-statutory licenses, whether they are 30, 60, or 100, are irrelevant to your inquiry. This is a statutory license proceeding. The economics are totally different between a statutory license setting and a non-statutory license setting.

All right. Moving back to the economic and relevant jurisprudence alluded to by Mr. Rich for a brief moment.

CHAIRPERSON VAN LOON: Mr. Steinthal, I'm sorry. I need to interrupt you for a minute. We are

caught in conflicting interests. On the one hand, we want to know and learn as much about this case as we can. On the other hand, we know that the whole operation is under tight time constraints. We agreed prior to today for two hours per side, cutting out the break time and all of that. Your five speakers have collectively now used that time.

I think that we have at least two possibilities. One is additional time for you now, providing additional time for the owners and performers, or cutting this off relatively quickly.

Can I ask in terms of your presentation, what additional --

MR. STEINTHAL: I can wrap up in five minutes.

CHAIRPERSON VAN LOON: Five minutes. Then would that be acceptable?

MR. GARRETT: I have no objection.

CHAIRPERSON VAN LOON: Okay. Thank you very much.

MR. STEINTHAL: Indeed I will just skip past a little part in the interests of getting there.

Let me conclude by focusing for one moment on the actual rate proposed by the RIAA, the four-tenths to five-tenths per stream or the 15 percent of revenue. We will demonstrate that these numbers bear no semblance of reasonableness either when viewed against other comparable intellectual property benchmarks or evaluated in the context of whether broadcasters and webcasters can effectively offer their services at all under such an economic burden.

Mr. Rich talked about the analogous musical works benchmarks. The evidence will show that the performances of musical works embedded in sound recordings, the performance of which are at issue in this case, are priced in the range of either three to three-and-a-half percent of revenues or less than a quarter of a cent per listener hour. Both these figures are multiples less than the fee sought by the RIAA.

One way to see how devastating and ludicrous the RIAA's proposal would be is through the following statistic. As Mr. Joseph stressed, sound recording performances are free for broadcast radio

precisely because of the enormous promotional benefit derived by the labels from the air play of sound recordings. Let us assume that everyone listening to terrestrial broadcast radio today started listening tomorrow to the same radio programming and the same radio stations, by via their PCs instead of their portable radios. Same programming, same audience. The RIAA's proposal, at four-tenths of a cent per performance, would yield a fee that is phenomenal, of more than $5 billion for that which is free today by transmitting by radio, terrestrial radio instead of on the Internet.

Now if you use a 15 percent of revenue number instead of a four-tenths of a cent per performance, it is still a staggering number, $1.7 billion for that which is free today because of the promotional value of air play, and the fact that congressionally, it has been determined that that is enough compensation for purposes of rewarding the sound recording owners and artists associated with air play on radio.

Now how can these figures be rationalized

under the DMCA? They can't. I urge you to reflect on the testimony of Professors Jaffe and Fisher and the history of the DMCA. As this evidence and the statutory history reflect, the very creation of the sound recording performance right was meant to protect the record labels from the loss of album sales that might derive from one of two different concepts, either from digital quality copying or a risk of substitution or displacement from on-demand types of transmissions.

Nobody really knew exactly how music would be transmitted in all its manifestations on the Internet. The compulsory license was created to give the labels the opportunity to be compensated in the event either of those two risks coming into play. It was decidedly not created to provide the record labels with a windfall of the nature they are seeking in this case, which bears no relation to either of the risks that the compulsory license was intended to protect against.

You will hear testimony from all the broadcasters and webcasters about how the RIAA rate

would make webcasting entirely uneconomic, and likely drive them out of business, the path of many of the RIAA's prior licensees.

So you may ask yourself, why would the RIAA seek such a high rate, so high that all of our clients might have to cease webcasting? It seems counter-intuitive, since some royalty, even at a lower rate, would seem better than none. Well, the answer is in a word that I heard from Mr. Garrett, control. It is not counter-intuitive if you keep in mind that another way to view this is as a matter of the label's desire to control the space as much as it is about the rate.

You will see the evidence that the major labels themselves are getting into the Internet music space. If they succeed in establishing a statutory license rate at or anywhere remotely near the one they are requesting, they will succeed in driving most of the existing non-label controlled webcasters out of this space.

That would be a horrible result to everyone, except the RIAA's major label members. It

would deprive the public of the types of choices that the DMCA was designed in part to give them. It would be bad for artists as well, in so far as it would limit the avenues for promoting their music other than on label-controlled websites. That is why we have two artists, including Alanis Morisette, testifying on our behalf. Of course, it would be devastating for all the broadcasters and webcasters participating in this case.

In concluding, we believe you will see that the RIAA's case is largely a charade. It purports to rely on a series of so-called willing buyer, willing seller transactions. But at the same time, the RIAA seeks to silence the willing buyers so that you can hear only one side of the story.

As a litigator, it frustrates me to no end that the truth is being buried beneath an avalanche of confidentiality clauses and under circumstances where there is no subpoena power. With subpoena power, the house of cards built by the RIAA around this self-selected tiny handful of deals would tumble instantly. But even without that tool, we will demonstrate to the

Panel's satisfaction that the RIAA's case is utterly lacking in substance.

Thank you for your time.

CHAIRPERSON VAN LOON: Thank you very much.

We knew at the outset and we discussed on June 25th that we had something of a marathon task ahead of us. That continues through today. There were a number of procedural matters that we wanted to take up and have some discussion of at the end of the day.

Do you want to take a brief recess before? Okay. We will take a very brief recess until about 5:50, and ask you to take a look at the list of issues that were provided by the Copyright Office staff last week.

(Whereupon, the proceedings went off the record at 5:41 p.m. and went back on the record at 5:51 p.m.)

CHAIRPERSON VAN LOON: We would like to add one short item to the top of our list for discussion. It is primarily in the form of a request,

Mr. Garrett, to you. We are aware of the discussion of the issue of confidentiality with NPR and Ms. Leary and her role and participation in this. We are interested obviously in having as full and complete a presentation of everything as we can. We are hoping that it might be possible for you and her to have some further discussions about whether there is some kind of practical format under which she could be enabled to participate, given NPR financial constraints and the rest, with a clear demarkation, some form of a firewall that would make you and your colleagues feel very comfortable in protections. This is really only in the nature of a request for a further conversation and exploration of possibilities in that regard.

MR. GARRETT: Certainly. If that is the Panel's wish, we will do that. I will only say that we did have those discussions before, and I thought that we had resolved them. There is an order or a stipulation that we had entered into filed with the Copyright Office that addressed that on July 11th, but if the sense of the Panel is as you have stated, I will be happy to talk with her again.

MR. VON KANN: We feel it is going to be awkward if she did today, and then somebody has got to bring her up to speed so she can comment. I think our inclination would be to see if she could be treated the same as any other, as if she were outside counsel, with whatever protections are necessary to effectuate that. We don't know the specifics.

MR. GARRETT: There is no intent here to single out Ms. Leary. I think our concern was broader. It is that we didn't want, and I don't think the other side wanted, in-house parties to be able to have access to this restricted material for very good and legitimate reasons. We live under that same rule because I would love to have the folks from RIAA here helping in assisting in the preparation of many of these things and we can't have that.

As I say, we did try to resolve it. I really thought until Ms. Leary had walked up earlier today, that we had resolved it to everyone's satisfaction in this July 11th order, but I will be happy to go back and take another crack at it.

MS. LEARY: I would note that I had a

conversation at the break with Hillary Rosen. When I first discussed this with Mr. Garrett, I had first raised it with Ms. Woods and then Mr. Garrett back right after the April cases were filed. I was told that they had checked with their labelers, and that the labels were unwilling to waive the restrictions. I offered to allow their counsel to have access to any portions of our case that were restricted. At that point, there were portions of the case that were restricted. They have all been removed, so that it was fair.

Ms. Rosen mentioned to me at the break that she was totally unaware that the circumstances existed. So perhaps conversations could be had with her by Mr. Garrett. But she seemed to want to do something to cure the situation. So perhaps Ms. Rosen was not consulted when Mr. Garrett was consulting his labels, but maybe that is an appropriate way to go now.

MR. GARRETT: I don't know who to believe more, the Panel or my own client. We're in a difficult position. Normally I am present when people

talk to my client about matters related to this, when other lawyers talk to my client about matters like this.

But as I said, I understand the sense of the Panel here. I will do my best to accommodate you.

CHAIRPERSON VAN LOON: Thank you very much.

We wanted to skip around on the list somewhat and in part talk about number three, the division of time, because we found among the Panel we had some different understandings of exactly what it was you might have in mind.

Perhaps we can hear from you first. What's the deal?

MR. JACOBY: We have discussed it. The announcement that was issued by the Copyright Office does not accurately reflect the understanding that was agreed upon, so that probably everybody is operating the same assumption when they read this.

The agreement was that we would divide the time equally, considering your own direct case and your cross examination of the other witnesses rather

than as stated here, where we are dividing the time based on your direct case, including the cross time by opposing side. That would give neither party the ability, neither side to control in effect.

MR. VON KANN: In effect, each of you owns a lectern for 90 hours?

MR. JACOBY: That is correct, for as much as we want to devote on our direct case or on the cross examination of the other side.

The second aspect of it, and I think most of these things then just clarify very quickly. We have calculated that as 90 hours, you may recall the calculation based on 30 days of hearings, assuming six hours per day for the examination and cross examination by the parties to the proceeding, assuming that there would be additional time taken with procedural matters as well as with any examination that the members of the Panel wish to do, which would take us beyond the six hours today. But we were assuming, you will recall, we I think talked about starting at 9:00 in the morning.

MR. VON KANN: Yes.

MR. JACOBY: That should give us a day that might run seven hours of hearing time or what, depending on how much procedural or arbitrator questioning might be involved.

The other aspect of it are that we had agreed that each side will essentially police themselves with respect to the various parties that might be involved in examination or cross examination. We are responsible as a side for those 90 hours, whether we have in some cases just one person cross examine a witness, in some cases there may be three or four. It depends on the matter and whether different interests or different people are taking care of different interest. But in the end, we pay the piper, because if someone takes more time than they should, we are going to end up, it is running against our clock.

Obviously, we have a very strong incentive on both sides not to overlap among cross examiners. If there are different cross examiners, that they try to be discrete as their subject matter, limit the extent of overlap to the maximum extent that we can to

avoid using up the clock.

CHAIRPERSON VAN LOON: Now is there a provision for each of you to be timekeeper for the other as well?

MR. JACOBY: We didn't come up with a solution. We had actually hoped that the court reporting service could provide that kind of a facility, but we have been told it could not.

CHAIRPERSON VAN LOON: They are really under the gun for an incredible marathon as it is. So I think putting additional burden there is not the best way to go.

MR. JACOBY: Well, there are technologies available to do it, but apparently the reporter who is involved here doesn't have those technologies.

In any event, what we have chosen to do again by discussion, would be that each side would designate each day one or more persons to serve as a timekeeper for that side, whether it be a legal assistant or attorney or what. I guess each day it may be someone different. But that we would each then keep a clock basically. Then at the end of the day,

the timekeepers would match up their records. If there is any discrepancy of any significance, then we will have to address it.

MR. STEINTHAL: We've got arbitration.

CHAIRPERSON VAN LOON: Mediation, hopefully.

MR. JACOBY: Hopefully it will be close enough so that we don't have to get involved in any ancillary proceedings with what the timekeeping is.

MS. WOODS: We do think we need to do it on a daily basis.

MR. JACOBY: Yes. It's a safe way. Whoever is designated at the end of the day will sit down with one another, see how it matches up. If there is a problem, then deal with it then or the next morning if we have to, but hopefully we won't have to do it at all.

CHAIRPERSON VAN LOON: I think it would be helpful also, just as a housekeeping matter, if either at the end of the day or perhaps first thing the next morning, somebody could give us a sheet that says here is where we stand.

MR. JACOBY: Right. We will create a running log on top of the daily I guess just to ensure that everybody is on the same page all the way through.

CHAIRPERSON VAN LOON: So if each has 90 hours and you choose to have 30 for your direct, then you have got 60 for your cross, and you will keep track of how it is divided among your colleagues.

MR. JACOBY: Yes. Ultimately, the total that we each have separately is 90 hours, whether questioning our own witnesses or questioning the other side's witnesses.

MR. VON KANN: Does the rule about or the provision about you can have as many cross examiners as you want apply also to direct? Or have you got a convention as to the direct only one attorney will put on a particular witness?

MR. JACOBY: We didn't actually discuss it. I don't know that there is --

MR. GULIN: Let's start with that premise. Are you saying that you can have as many cross examiners as you want on your side?

MR. JACOBY: Yes. I guess each side can make a decision if in fact there are different interests, there are different parties that have different interests here. A particular witness may generate issues that different people are addressing.

MR. GULIN: Clearly, there are some parties with different interest within your group. But it seems like we are heading towards a situation where we are only having two sides here. We are going to identify exhibits either as copyright owners, performers versus services. I am not sure we can do that. Can we, in this proceeding? I mean aren't you going to want to identify who is representing what parties? When we put an exhibit into evidence, shouldn't it be identified by that party who is doing the cross examination?

In other words, it seems to me that it might be helpful to have a little more structure to this, to have maybe an order of who are the groups that are cross examining rather than simply say you may throw 40 at one witness, and you may have ten for a different witness.

MR. JACOBY: No, we are not going to do that. We are not going to do that.

MR. GULIN: Well are you saying that you may have two attorneys representing the same party doing cross examination?

MR. JACOBY: There may be broadcaster interests on particular issues that are somewhat different from the webcasters. You have the NPR interests. You have the business establishment group. In some cases, they may have different interests to pursue in a cross examination. Theoretically, you could have several people cross examining. The same is true on the RIAA.

MR. GULIN: I guess what I'm saying is would it be helpful and useful to identify who these groups are now so that when the time comes for an attorney to do a cross examination, we will know who that attorney is representing, who his parties are, so that we can identify witnesses properly, rather than willy nilly kind of cross examination.

MR. STEINTHAL: I think that it's easy enough with respect to NPR and Wiley Rine, and even

David and Sandra in terms of that part of the DMX AEI case. I think it is a little bit more difficult, although we are going to try to segregate it, I mean I have been more involved in the "webcaster" side. Bruce Rich has been more involved on the broadcaster side, but the experts obviously span both. So it is hard for us to say we are affiliated with this group and not that group.

So I think we can identify certainly exhibits by group. I mean I don't see why we can't just use a sequential numbering in broadcaster, webcaster exhibits, you know, one through whatever. If it turns out that it is a clear channel document, then it will just go into clear channels post trial findings with a broadcaster, webcaster exhibit number. I mean I don't know why that --

MR. JACOBY: I guess the first question really is what is the significance in terms of how you designate exhibits? We could just have SG service group generally for the numbers and go one, two, three, four. If it's admitted into evidence, it's in evidence in the proceeding.

CHAIRPERSON VAN LOON: We know we have the cops over here, the copyright owners and performers.

MR. GARRETT: That's true. I like the acronym.

CHAIRPERSON VAN LOON: You have had, I think, suggestion.

MR. GARRETT: I was just going to say we have already started marking all of our exhibits as RIAA exhibit, not as copyright owners and performers exhibits. I had certainly contemplated, unless this is a problem for the Panel, to continue to mark our exhibits as RIAA exhibits. Should any of my colleagues introduce anything in their cross examinations and they would mark it AFTRA or AFIM or AFM, as the case may be.

Let me also say we don't have an objection to having multiple parties cross examine, but there is a limit to that. We recognize that they may have different and distinct interests on the other side of the table. If there is a matter that affects one group differently than the other, then those two groups should both have the right to cross examine.

It is going to come out of their 90 hours. But on the other hand, if there really isn't a basis to distinguish and it's just ganging up on one witness here, having somebody go 15 hours and let them be a tag team, that's not something we are agreeing to.

MR. GULIN: Trial strategy enters into this. That is why I think it is relevant to say how many rounds of cross examination are appropriate for a given side based upon how many different interest that side has.

Now I think you started out by saying you don't have any objection to them simply marking their exhibits as services, the services exhibits in cross examination, but you do have a problem with some type of limitation on the number of rounds of cross examination. Can we get from your side some idea of how many different separate and distinct interests are there within your side? I think it would be fair, would it not, to limit you to that number of rounds of cross examination?

MR. JACOBY: The maximum it conceivably would be is four. I can assure you that for the vast

majority of witnesses, we are not going to have four.

MR. VON KANN: The four are webcasters, broadcasters, business services, and NPR?

MR. JACOBY: Correct.

MR. VON KANN: There really are those four components.

MR. JACOBY: That's right.

MR. VON KANN: Is there any problem, maybe it doesn't make a problem, if your exhibits come in sort of blanket, and then NPR is sort of stuck with some exhibit that maybe came in from somebody else that isn't really particularly helpful to them. Should these be segmented a little bit, NPR's exhibits, webcasters, broadcasters, services, or whatever, business.

MR. JACOBY: I guess if they all agree that they want to have all their exhibits and be bound by each other's exhibits, that is fine, but it seems like it could create some legal problems for some of the parties.

MR. GULIN: Maybe it's not an issue.

MR. JACOBY: I think we have over reacted.

If they are in the record, they are in the record. If they are valid evidence, you will have to make a decision as to what they are valid. If a particular party, for example, if something is put in by the broadcasters and webcasters and NPR says that's fine, but that is not relevant to our situation, they will be able to say that in their briefing. It is still in the evidence in the total record of the case. You are not creating separate records for different parties. You may be issuing different rates for different parties.

MR. GULIN: So that this point, you can't foresee a situation where an exhibit might be helpful to one party but detrimental to another party within your side?

MS. LEARY: No. If we saw the need for a conflict, I think we would really raise that very early on.

MR. GULIN: How would we resolve it? If we have been naming all the exhibits as the services exhibits?

MS. LEARY: Services exhibit, except not

sponsored by public radio, something like that.

MR. JACOBY: Just note on the record if such a situation arose.

CHAIRPERSON VAN LOON: It sounds like as a practical matter you don't anticipate that arising and this is the way that we could deal with it if it were.

MS. LEARY: The litigation with the RIAA is our chief focus rather than the lateral argument on this side.

MR. GARRETT: They are all united in hating us.

(Laughter.)

MR. VON KANN: Can we move back to Mr. Garrett's point about ganging up? I think we may need -- it strikes me that we might need to talk about that a little bit.

I could see a situation in which Steve Marks comes along and you decide to devote 30 hours to cross examining him. One after another, everybody on this side of the room that can think of anything to ask Steve Marks asks it, and you decide to really make

-- if that is within your contemplation, that is I guess your deal. I am not sure we would interfere with it.

MR. JACOBY: As we said, there is really an maximum of four interests on our side. There are four parties at the table on the other side. Frankly, the suggestion of doing that kind of teaming up will be opaque to you and will not be appreciated. The same would be true if the other side did it to our witnesses.

MR. VON KANN: Do we need to have a rule or an understanding that only one attorney for each of those four components will be permitted to cross examine? So if one of you gets up and you are from the webcaster group, you can't put three more webcaster attorneys in there to talk about. You can have one webcaster guy and one broadcaster, and one service whatever.

MR. RICH: It strikes me, if I may, that this is a situation where the adage "if it ain't broke, don't fix it," may come into play. I suspect there won't be any abuse of it by either side.

MR. JOSEPH: There are two different firms representing radio broadcasters. We are certainly coordinating. We are going to make every effort to make sure that we coordinate.

CHAIRPERSON VAN LOON: I suspect that the discipline of the 90 hours is going to eliminate enough.

MR. GULIN: Can we agree though that there is a maximum of four rounds of cross examination per side? It seems to apply to both sides?

MS. WOODS: And Judge Gulin, I take it by four rounds you mean four cross examiners. I guess we had previously termed as single round --

MR. GULIN: I'm sorry. I mean four different cross examiners of the same witness within the same round of cross examination.

MS. WOODS: We do contemplate the possibility of redirect and recross, which we have had in previous proceedings.

MR. JACOBY: I think we agreed that redirect and recross would be more than you would want to bear. Beyond that, someone better have an

extraordinary reason for asking permission.

MR. GULIN: So we are going to identify exhibits on this side as the services.

MR. JACOBY: SG, is that all right? SX? SX.

MR. GULIN: Love it.

MR. JACOBY: Fill in the blanks. SX, 1, 2, 3. Then if there's a problem with one --

MR. GULIN: Okay. You still want to maintain your integrity over here with respect to individual names?

MR. GARRETT: I have never been accused of having that much integrity before. I think yes. If we start, I don't want to be too narrowly focused on this, but I mean we started out labeling everything RIAA exhibit, and then we gave it D for direct case and either a P for a public exhibit, or R for restricted, so that we can easily identify which exhibits are restricted, which ones are public. What we will simply do is add an X to that numbering system here.

Let me also say that I don't think there

is anything that we are proposing here that limits the authority of the Panel here under section 251.47(j) to limit cross examinations where in your judgement you thought it was cumulative or caused undue delay. I suspect all of us would want to be free to make the argument that this is now a second or a third round of cross examination from someone who really does not have a separate interest in what they are doing.

MR. VON KANN: Or even if they do have a separate interest, we have heard enough.

MR. GARRETT: Exactly.

MR. VON KANN: At some point cumulative and duplicative cross examination has to be cut off, no matter what their interests are.

MR. GARRETT: To accommodate everyone on Mr. Marks, I will plan only a 15 minute direct exam so that he is in good shape.

CHAIRPERSON VAN LOON: Great.

MR. VON KANN: Can we pick up just one thing that Mr. Rich said that I think is worth just briefly noting? That is, that the Panel is very pleased that you all have been able to generally work

this out by agreement. As much as possible, we do not intend to tamper with or upset any deals that you have worked out. We just want to understand what they are.

MR. RICH: At the same time, you know none of us is shy to bring issues.

MR. VON KANN: We are delighted, and we hope that will continue on as many of these kind of administrative matters as you can reach agreement on. Our inclination is to try to support that as much as we can.

CHAIRPERSON VAN LOON: Absolutely.

Also, in the administrative vein, we noticed with regard to the motion that was filed on the 27th with regard to limiting portions or confidentiality, you appear to have a pretty carefully thought out schedule of witnesses that goes down through August 13th and who you think will be on on what day. It would be very helpful to us to know on the one hand sort of the master plan, and then at least on the start of each Monday morning or whatever, here's the adjustments, if any, that we know about for the week. Obviously we want to stay flexible, but it

can also be very helpful to us and everybody I think to know who is contemplated. Thank you very much.

Related to the overall question of the 90 hours, we thought it only fair to share with you our tentative thinking on the death march of the schedule.

MR. VON KANN: Can I just ask one question about the paper we just got?

CHAIRPERSON VAN LOON: Oh yes, the 17th.

MR. VON KANN: Why is the 17th blank?

MS. WOODS: That just means that RIAA expects to finish its case on the 16th, so we would expect witnesses from the other side to start on the 17th, and we don't know their schedule.

MR. VON KANN: Excellent. Okay.

CHAIRPERSON VAN LOON: We are anticipating in order for you to be sure to each get your full 90 hours and for us to have some small questioning, but to have adequate time for discussion of these procedural type matters, that we have been thinking about a tentative sort of presumptive schedule that would produce about seven hours a day of quality time together. Actually seven hours for testimony and 15

minutes for procedure. It is in a framework that would start at 9:00 and end at 6:00. We would like to put this out for you to reflect on and give us reactions.

We wanted to start promptly at 9:00 each morning. We are thinking in terms of taking the first 15 minutes for procedural matters, announcements, administrative housekeeping, so that we all know sort of whether there are changes for the day.

And that we would plan to have the first testimony block go from 9:15 to 10:30, with the idea of a 15 minute break at that point. Then going 10:45 to 12:15. Then breaking for lunch for an hour, 12:15 to 1:15. With the next testimony block being 1:15 to 2:30, with a 15 minute break. Then 2:45 to 4:15, and another break, 15 minutes. Then 4:30 to 6:00.

Obviously this is not meant to be ridiculously rigid. We want to have ebb and flow with who is on the stand and where we are, but with the idea that clearly we will need a morning break and a couple afternoon breaks if we are going to keep to this kind of a heavy schedule. We were thinking an

hour for lunch rather than longer would be appropriate.

Without putting anything in stone today, we are interested in whether you have any reactions or thoughts one way or the other about this.

MS. WOODS: We had actually discussed the possibility of 45 minute lunch to make things move along, but we thought an hour with phone calls and everything was probably what was needed.

CHAIRPERSON VAN LOON: We were informed that cell phones don't work in this building and there are no pay phones. So it's well designed to keep our nose to the grindstone.

Again, that will be sort of our working model, but you certainly are welcome if you have additional thoughts after reflecting on it over night to bring that to our attention.

MR. GARRETT: Just one question, Mr. Chairman. As I say, we passed out this schedule here. This is what we have told all of our witnesses would be the schedule. We had shared this with the webcasters earlier too. I don't know if we will ever

have a situation where we might finish with somebody at 3:00, and then we won't have somebody available until the next day because a lot of people are flying across country and most all of our witnesses are from out of town. But I don't want to incur the wrath of the Panel if we finish with a witness at 4:00 and we don't have another one to go on right away.

CHAIRPERSON VAN LOON: If that were to happen on a Friday, I can assure you it would not incur the wrath.

(Laughter.)

MR. GARRETT: It is usually the cross examiners who make that determination.

MR. JACOBY: I think the only problem there is that if you haven't planned adequately to have backup there, the issue is whose clock is running at that point? Since we have a limited amount of time, there is an unfairness that could apply to either side in that situation if you don't have a witness ready, your next witness ready.

CHAIRPERSON VAN LOON: At the same time, you are each at the other's mercy in the sense of how

long the witness is going to go, really will depend in significant measure on the amount of cross.

Perhaps what we might do is start with this as a framework. Let's see whether we get into periods, or I don't know whether other panelists have a reaction.

MR. VON KANN: We were just actually talking at lunch about I remember trying cases some of you have in Montgomery County, where if you finished at 5:15 with your witness, the judge said "Call your next witness. We have 15 minutes." I don't think it would be a problem if occasionally we finished. But if day after day, then the 90 hours per side is going to push us well past whatever cutoff date, September 13 or 14, we have targeted. So that's where you could run into a problem.

CHAIRPERSON VAN LOON: It's September 13th, and there is not flexibility.

MR. GARRETT: I appreciate that. I certainly don't want to be the one to jam up the works here. But we made our best good faith effort here to identify how much time we thought each witness would

be on. We shared this with the webcasters a while back. We don't have any feedback from them on how long their cross examination is going to go.

For example, we have somebody who is coming in from out of the country and will be arriving at a particular time, and would be obviously not prepared to go.

I am happy just to play it by ear. I just want you to understand.

MR. VON KANN: Have you told them about how long you expect your direct of each of these witnesses to be?

MR. GARRETT: No. We have not had any conversations. We sent them our --

MR. VON KANN: This sounds like Alfonse and Gaston. Who first indicates how much time we are going to take with direct or cross. We could have a certain simultaneous exchange.

MR. JACOBY: Well, I think the issue there is direct testimony in written form we have. It is a question of how much time either party chooses to take with its direct witness here live obviously. You may

choose not to cover every aspect of what they had in their written testimony, for whatever reason.

I think looking at the schedule, I mean we understand the practicalities. We have the same problems in terms of witnesses coming in from across the country and what have you. I think the only thing that gives us a little bit of concern looking at the schedule is this particular schedule is somewhat backend loaded with witnesses who are likely to require more cross examination than less, because you have got Mr. Marks and then three experts. Whereas, for example, the date before that is Jennifer Warnes, who I'm sure will give us a wonderful rendition, but I am not sure how extensive the direct or cross will give, and Mr. Bradley.

CHAIRPERSON VAN LOON: You need a lot of time with Mr. Guitar.

MR. JACOBY: Unless they are going to get together to do a duo, but if that is the case, we ought to schedule that for Friday.

MR. STEINTHAL: Then maybe Steve can be available to start on Monday.

MR. JACOBY: Steve is someone who is local.

CHAIRPERSON VAN LOON: Do you think that that is a possibility?

MR. GARRETT: I am sure that would cause no problem at all. I am more concerned about witnesses who are coming from different parts of the country.

MR. JACOBY: I think your initial suggestion of maybe we see how it goes. If we don't get out of whack then the first few days, we can probably just live with this until such time we see a problem.

CHAIRPERSON VAN LOON: And with regard to the big picture, assuming you are in a position to start either the afternoon of the 16th or probably more likely the morning of the 17th, that works for you, the way that you planned your sequence of witnesses?

MR. JACOBY: Yes. We are tentatively fleshing out a schedule. Obviously we needed theirs first. It may change based on their schedule because

we may decide even as a tactical matter to change. But we have provided a batting order. Now we are trying to slot those people in on the days based on, make sure that the availability coincides with what we anticipate here. Of course anything that changes on either side, I think we understand, notify the other side immediately if there is going to be a change in the schedule.

MS. WOODS: May I ask, if are going to that, I will be taking the chief scheduling role for this side. May I ask who will be doing that?

MR. JACOBY: I don't know, but we will designate someone.

MS. WOODS: That would be helpful so we could just --

CHAIRPERSON VAN LOON: I agree. I think that's imminently practical.

MR. VON KANN: Have you all discussed between yourselves the extent to which you want to telescope considerably the presentation of direct? I mean as has been pointed out, it has all been presented in writing. We have all read it. All three

of us have read all the testimony of all the witnesses. I can't say we have mastered it completely, but having somebody read it to me again will probably not help that much.

It does strike me this is going to be a case that the cross examination is going to be much more significant on both sides than spending a whole lot of time rehashing what you have already given us in writing.

So I don't know whether you all were envisioning quite brief presentations on direct or quite extensive ones. I guess that is something for you all to think about.

MR. JACOBY: Again, it is part of the process of dividing up respectively our own direct and how much time we want to leave for cross.

CHAIRPERSON VAN LOON: Are there other administrative matters or issues that we ought to discuss tonight?

MR. GULIN: We have the issue of the delegated motions. Has that been mooted? The Yahoo matter. Is that now moot?

MR. GARRETT: Yes.

MR. JACOBY: That is on the record.

So I want it to be imminently clear, lest someone think otherwise. They have waived, as I understand it, the non-cooperation provisions of the Yahoo agreement.

MR. GULIN: So that motion is withdrawn.

MR. KIRBY: I was just wondering if they had informed Yahoo of the waiver or given us something we can provide to Yahoo concerning the waiver.

My name is Tom Kirby, I'm sorry.

MR. STEINTHAL: The question is whether there can be something on the record so that Yahoo can be so informed with a piece of paper reflecting that the motion has been mooted by their consent. Unless Bob objects, then we will get a page of this transcript, and that will be the record of it.

MR. JACOBY: Or you might just want to do a one or two sentence letter saying that. That way, we don't have to worry about waiting for the transcript or any issues like that.

MR. GARRETT: I can send a confirming

letter.

MR. JACOBY: A confirming letter signed.

MR. GARRETT: Fine. I'll do that.

MR. GULIN: And we would like a copy of it, please.

MR. GARRETT: No problem.

MR. GULIN: And then the remaining issue was in the agreement being reached with respect to the use of documents on cross examination.

MS. WOODS: We discussed that matter, and pretty much thought we would need to leave it case by case as the situations arise. We thought that the 90 hour limitation would likely cut down a lot on sort of general reading of documents on cross examination, but we thought really we didn't have guidelines to agree to, so we just have to wait.

CHAIRPERSON VAN LOON: Okay. We may want to discuss that with you further, depending on how that plays out in our further discussion.

It has already been a longish day, even though we didn't have to have lunch here in the library to launch this process. Are there any other

urgent matters before we adjourn, to see each other right back here at 9:00? We'll look forward to seeing you then.

I'm sorry. I guess Mr. Garrett has one.

MR. GARRETT: As I understand it, I have been told that there will be more counsel tables provided for us, that that may not occur until tomorrow morning. So there may be some delay in getting started.

CHAIRPERSON VAN LOON: There is one other very important housekeeping matter. This is literal. Apparently, unlike in probably your offices and ours, there is not a crack team that comes through and cleans up cups, bottles, paper scraps, things of that nature. So we have to pretend we are in a national park. True housekeeping. Please leave no trace. You will want your table to look so wonderful and when you walk in tomorrow.

MR. STEINTHAL: Where will the witness chair be?

CHAIRPERSON VAN LOON: That is the usual setup. The witnesses over here then.

COURT REPORTER: One last question.

CHAIRPERSON VAN LOON: One last question.

COURT REPORTER: What happens to all these opening statements? Do they get bound in? Some are confidential, some are public. Do you want them bound in?

MR. STEINTHAL: Why don't we just leave them.

MR. JACOBY: None of it is evidence, obviously in the opening statement.

CHAIRPERSON VAN LOON: I agree. We all have our copies.

MR. JACOBY: It's demonstrative. It's not evidence.

CHAIRPERSON VAN LOON: Okay. Excellent. Thank you very much.

(Whereupon, the proceedings adjourned at 6:32 p.m., to reconvene at 9:00 the following morning.)

CERTIFICATE

This is to certify that the foregoing transcript in

the matter of:	Hearing: Digital Performance Right in Sound Recording and Ephemeral Recording, Docket No. 2000-9 CARP DTRA 1 & 2
Before:	Library of Congress Copyright Arbitration Royalty Panel
Date:	July 30, 2001
Place:	Washington, DC

represents the full and complete proceedings of the aforementioned matter, as reported and reduced to typewriting.